United States Court of Appeals

for the Second Circuit



BRIEF FOR APPELLEE

Signed

76-4216

IN THE UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

IRVING I. RUSOFF AND PERLE P. RUSOFF;
ROBERT STRICKMAN AND ROSE STRICKMAN;
WILLIAM W. SUITT AND KATHRYN S. SUITT;
ROBERT S. RAUM AND RUTH RAUM; and
IRVING I. RUSOFF AND PERLE P. RUSOFF,

Appellants

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee

ON APPEAL FROM THE DECISIONS

OF THE UNITED STATES TAX COURT

BRIEF FOR THE APPELLEE

B
P/S

MYRON C. BAUM,
Acting Assistant Attorney General,

GILBERT E. ANDREWS,
LEONARD J. HENZKE, JR.,
PHILLIP I. BRENNAN,
Attorneys,
Tax Division,
Department of Justice,
Washington, D.C. 20530.

UNITED STATES COURT OF APPEALS
FILED
DEC 29 1976
A. DANIEL FUSARO, CLERK
SECOND CIRCUIT

TABLE OF CONTENTS

	Page
Statement of the issues presented	1
Statement of the case	2
Summary of argument	10
Argument:	
The Tax Court correctly concluded that taxpayers' transfer of invention rights to Columbia University was a sale and not a deductible charitable contribution	13
A. Introduction--A transfer is not a deductible contribution if the transferor receives substantial material quid pro quo benefits, or if he has no donative intent	13
1. The quid pro quo requirement	15
2. The charitable or donative intent requirement	18
3. The Government's position on the relationship between the Section 170 requirements	19
4. The standard of appellate review	20
B. The Tax Court properly concluded that taxpayers' transfer satisifed neither the quid pro quo nor the charitable intent tests under Code Section 170	21
1. The Tax Court correctly disallowed the charitable contribution deduction because the transfer constituted a quid pro quo, bargained for sale of the invention	22
2. The Tax Court also correctly disallowed the charitable contribution deduction because the transfer was not motivated by the requisite charitable intent	27
C. The Tax Court correctly held that no part of the value of the invention constituted a charitable contribution under a bargain sale theory	31
Conclusion	32

Page

Appendix A---------- 34
Appendix B---------- 1a

CITATIONS

Cases:

Beck Industries, Inc., In re, 479 F. 2d 410 (C.A. 2, 1973)---------- 20
Biedenharn Realty Co. v. United States, 526 F. 2d 409 (C.A. 5, 1975), cert. denied, 45 U.S. Law Week 3249 (Sup. Ct., Oct. 4, 1976)---------- 20
Central Tablet Mfg. Co. v. United States, 417 U.S. 673 (1974)---------- 24
Citizens & Southern National Bank of S. C. v. United States, 243 F. Supp. 900 (W.D. S.C., 1965)---------- 17
Commissioner v. Duberstein, 363 U.S. 278 (1960)------ 18
Commissioner v. Nat. Alfalfa Dehydrating, 417 U.S. 134 (1974)---------- 24
DeJong v. Commissioner, 309 F. 2d 373 (C.A. 9, 1962)- 18,20,27
Dempster Brothers, Inc. v. Buffalo Metal Container Corp., 352 F. 2d 420 (C.A. 2, 1965)---------- 21
Grinslade v. Commissioner, 59 T.C. 566 (1973)-------- 16, 31
Oppewal v. Commissioner, 468 F. 2d 1000 (C.A. 1, 1972)---------- 14,19.20
Orvis v. Higgins, 180 F. 2d 537 (C.A. 2, 1950), cert. denied, 340 U.S. 810 (1950)---------- 20
Perlmutter v. Commissioner, 45 T.C. 311 (1965)------- 16, 18
Pettit v. Commissioner, 61 T.C. 634 (1974)---------- 17, 18
Rainier Companies, Inc. v. Commissioner, 61 T.C. 68 (1973), rev'd in unpublished opinion (C.A. 9, Nov. 5, 1975)---------- 27
Reyher v. Children's Television Workshop, 533 F. 2d 87 (C.A. 2, 1976)---------- 20
Sedam v. United States, 74-1 U.S.T.C., par. 9442, rev'd 518 F. 2d 242 (C.A. 7, 1975)---------- 15, 16
Singer Co. v. United States, 449 F. 2d 413 (Ct. Cl., 1971)---------- 16,17,18
Stubbs v. United States, 428 F. 2d 885 (C.A. 9, 1970)---------- 16, 18
Sutton v. Commissioner, 57 T.C. 239 (1971)---------- 16
Television Industries, Inc. v. Commissioner, 284 F. 2d 323 (C.A. 2, 1960)---------- 24
Turner v. Commissioner, 76-2 U.S.T.C., par. 9660 (C.A. 4, May 6, 1976), rev'g and remanding, 33 T.C.M. 1165 (1974)---------- 20
Union Planters Nat. Bank of Memphis v. United States, 426 F. 2d 115 (C.A. 6, 1970), cert. denied, 400 U.S. 827 (1970)---------- 20

Page

Cases (continued):

United States v. Aluminum Co. of America, 148 F. 2d 416 (C.A. 2, 1945)---------- 30
United States v. Transamerica Corp., 392 F. 2d 522 (C.A. 9, 1968)---------- 15, 18
Winters v. Commissioner, 468 F. 2d 778 (C.A. 2, 1972)---------- 14, 20

Statutes:

Internal Revenue Code of 1954 (26 U.S.C.):
Sec. 170---------- 13, 34
Sec. 1235---------- 4, 8

Miscellaneous:

Rev. Rul. 63-73, 1963-1 Cum. Bull. 35---------- 29
Senate Hearings before a Subcommittee of the Committee on Finance on Reviewing Progress Made Toward the Development and Marketing of a Less Hazardous Cigarette, 90th Cong., 1st Sess.---------- 30

IN THE UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 76-4216

IRVING I. RUSOFF AND PERLE P. RUSOFF;
ROBERT STRICKMAN AND ROSE STRICKMAN;
WILLIAM W. SUITT AND KATHRYN S. SUITT;
ROBERT S. RAUM AND RUTH RAUM; and
IRVING I. RUSOFF AND PERLE P. RUSOFF,

Appellants

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee

ON APPEAL FROM THE DECISIONS

OF THE UNITED STATES TAX COURT

BRIEF FOR THE APPELLEE

STATEMENT OF THE ISSUES PRESENTED

1. Whether the Tax Court correctly concluded that taxpayers[1/]' assignment of an invention to Columbia University was not a deductible charitable contribution under Section 170 of the Internal Revenue Code, on the ground that (1) the assignment constituted a bargained for sale for which taxpayers received significant material quid pro quo benefits; and (2) in any event,

---

1/ References to "taxpayers" are to Messrs. Rusoff, Strickman, Suitt and Raum. The other appellants are their respective wives, and are parties hereto only by reason of their having filed joint returns with their respective husbands. Mrs. Raum had died prior to the date of the Tax Court's opinion. (Op. 4, App. B, infra, p. 25a.)

the assignment was not motivated by the requisite subjective donative intent.

2. Whether the Tax Court correctly held that the assignment could not constitute a deductible contribution to the extent it might represent a bargain sale, since the requisite subjective donative intent was absent.

STATEMENT OF THE CASE

This case involves approximately $37,000 in income tax deficiencies for the years 1967 through 1969. (App. B,[2/] pp. 51a-60a.) The Tax Court (Judge Featherston) filed its opinion on December 2, 1975, which is reported at 65 T.C. 459, and entered its decisions on June 30, 1976. (App. B, pp. 51a-60a.) Jurisdiction is conferred on this Court by Section 7482 of the Internal Revenue Code of 1954.

The relevant facts as found by the Tax Court, supplemented by a few undisputed record facts, may be summarized as follows:

In the late 1950's one of the taxpayers herein, Robert Strickman, began the development of what was to become known as the Strickman Cigarette Filter--a filter designed to reduce the nicotine and tars from cigarette smoke. An application for a patent on the filter was filed on September 28, 1960, and was eventually granted on November 9, 1971. (Op. 4-5, App. B, pp. 25a-26a.)

During the filter's developmental stage, Strickman transferred undivided percentage interests in it to the other

---

2/ "App. B" references are to the portions of the record incorporated in Appendix B to this brief.

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

taxpayers and several other persons,[3/] either as compensation for assistance in developing the filter or as gifts. (Op. 5, App. B, p. 26a.)

In early 1967, taxpayer Suitt, a marketing consultant who had some knowledge of the cigarette industry and who saw an economic potential in the filter, brought together Strickman and Robert Katz, an attorney. Katz was given a scientific demonstration of the filter and concluded that its economic potential was "astronomical." He recommended that the rights to the filter be transferred to an organization which would be more capable than they in dealing with the powerful tobacco manufacturers. Such an organization, he advised, could more effectively negotiate licensing agreements with the tobacco industry. (Op. 5-6, App. B, pp. 26a-27a.)

Katz suggested that the transfer be made to the Medical School of Columbia University. Several doctors associated with that institution lived in Katz's community and some of them had been instrumental in saving the life of Katz's son several years earlier. Katz's contacts would facilitiate Columbia's acceptance of the transfer. Columbia was thus readily and quickly available as a desirable transferee, and it had the facilities to further develop the filter.

3/ Many of the part owners of the invention are not parties to this suit. Often in this brief, however, the owners will be referred to as "taxpayers", without the qualification that taxpayers do not constitute all the owners.

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

Since the other owners of interests in the filter had no objection to an arrangement with Columbia, negotiations with Columbia regarding the transfer were initiated. Katz, who represented the owners of the filter, informed Dr. Donald Tapley, a neighbor and faculty member of the medical school, about the filter and the desire of its owners to transfer it to Columbia. Dr. Tapley contacted William Bloor, treasurer of Columbia, who initiated proceedings within the University necessary for a transfer of the filter. On April 25, 1967, and May 4, 1967, meetings were held between representatives of the Strickman group and Columbia. (Op. 6-7, App. B, pp. 27a-28a.)

The participants at these meetings discussed the nature of the invention; the patent status of the invention; the tax considerations for the owners of interests in the filter[4/]; the nature of possible licensing arrangements between Columbia and the cigarette manufacturers, including royalty charges; proposed provisions of an assignment agreement between taxpayers and Columbia, including amounts referred to as a "purchase price to be paid periodically * * * which payments would be contingent on the amount of royalties received from the University's licensees;" and obligations which Columbia would undertake with respect to the filter. (Op. 7-8, App. B, pp. 28a-29a.)

4/ At the April 25, 1967, meeting, the applicability of Section 1235 of the Internal Revenue Code (26 U.S.C.) was discussed. That section, if applicable, would recognize payments received by taxpayers as gain from the sale or exchange of a capital asset.

DEPARTMENT OF JUSTICE
PHOTO OF EXACT COPY FILED

Katz felt, however, that its exploitation within the powerful tobacco industry and future licensing agreement negotiations could best be carried out by a large prestigious organization. Because of his contacts in the Medical School of Columbia University, he recommended that the rights to the filter be transferred to that institution, which possessed both the organizational capacity to exploit the filter and the research facilities to further develop it. (Op. 5-6, App. B, pp. 26a-27a.)

By June 8, 1967, the taxpayers and the other filter owners had grown to 20 [5/] in number, and it became apparent that such a large group could not efficiently and conveniently conduct negotiations with the University leading to a transfer of the filter without creating utter confusion and possible legal entanglements. [6/] Accordingly, on June 9, 1967, the owners, on the recommendation of Katz, executed a trust agreement whereby they transferred their respective interests in the filter to a trust which, through its two trustees, Strickman and Raum,

---

5/ During the development of the filter, certain of the original owners transferred part of their interest therein--either in the form of gifts or as compensation--to other individuals, trusts or companies. (Tr. 152-153.)

6/ In a letter dated June 6, 1967, to John Wheeler, an attorney for Columbia, Katz described the need for a trust as a vehicle for the transfer as follows (Op. 8, App. B, p. 29a):

> The Declaration of Trust will give to the Trustees legal title with all of the powers requisite to whatever action may be required in the future as well as the power to sell the patent to Columbia * * *. (Emphasis added.)

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

thereafter conducted all negotiations with the University. (Op. 8-9, App. B, pp. 29a-30a; Taxpayers' Br. 12-13.)

Pursuant to the trust, the trustees were to "collect the net income or proceeds of sale" and make distributions thereof to the grantors in accordance with their percentage of ownership. The powers of the trustees were described in part as follows (Op. 9, App. B, p. 30a):

TRUSTEES' POWERS

> 1. To sell to COLUMBIA UNIVERSITY or to any of its designess the entire rights, title and interest in and to the INVENTION upon such terms as in their sole discretion and judgment may be deemed for the best interest of the beneficiaries hereunder.

The University's understanding of what it was to receive from the taxpayers and other owners of the filter pursuant to the transfer was embodied in a report of the University's finance committee evaluating the advisability of consummating the transfer. The report read in part that (Op. 10, App. B, p. 31a):

> The holders of the invention would assign all of their rights, title and interest in the patent application to the University * * * in exchange for a purchase price * * * to be paid periodically over a period * * * [approximately] the life of the patent, which payments would be contingent on the amount of royalties received from the University's licenses * * *.

On July 7, 1967, an assignment by the trust of all its interest in the filter to the University and an assignment

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

agreement between the trustees and the University was executed. The agreement stated in part (Op. 11, App. B, p. 32a):

> Assignors [trustees] by these * * * present do hereby sell, assign and transfer unto Assignee [University] the full and exclusive right * * * in * * * the Invention * * *. (Emphasis added.)

The agreement went on to further state (Op. 12-13, App. B, pp. 33a-34a):

> Assignee [University] shall pay to the Assignors [trustees] as compensation for the assignment of the Invention and other considerations expressed herein, the following percentage of net royalties 7/ received by it from the licensing of the patent and trademark rights:
>
> | | |
> |---|---|
> | Out of the first $5,000,000 | 90% |
> | Out of the second $5,000,000 | 80% |
> | Out of the third $5,000,000 | 70% |
> | Out of the fourth $5,000,000 | 60% |
> | Out of the fifth $5,000,000 | 50% |
> | Out of all above $25,000,000 | 59% |
>
> [Emphasis added.]

Other obligations assumed by Columbia included the duty to negotiate nonexclusive licenses of the invention with cigarette manufacturers (Op. 11, App. B, p. 32a); to defend the patent through defensive and offensive litigation, if necessary; and

---

7/ Net royalties were defined in the agreement as the difference between gross receipts and expenses such as research, litigation, maintenance of patents and any other expenses incurred in developing the invention and maximizing its economic return. (Op. 12, App. B, p. 33a.)

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

to secure and maintain any desirable foreign patents (Op. 13, App. B, p. 34a). The agreement was to expire at the close of the calendar quarter in which the last of all the relevant patents expired, unless terminated earlier. The agreement described circumstances in which either party might choose to terminate the agreement: (1) In the event Columbia failed to comply with any provision of the agreement and such failure or breach continued uncured for a period of 60 days after written notice of the breach is received from the trust; and (2) in the event annual net royalties did not average at least $100,000 per year for any 3 consecutive calendar years beginning with 1971. If termination occurred, Columbia would reassign all rights in the invention to the trust. (Op. 13, App. B, p. 34a.)

The language of "sale" contained in the agreement was inserted to substantiate taxpayers' claim for "sale or exchange" treatment under Section 1235 on their gain on the disposition of the patent. The tax treatment of the net royalty payment to the trust had been the subject of discussion at negotiations between Columbia and taxpayers. In view of the concern that the payments be taxed at capital gains rates, no charitable deduction was anticipated at this time. The availability of a charitable deduction was not one of the reasons for approaching Columbia.[8/] (Op. 13-14, App. B, pp. 34a-35a.)

8/ On July 13, 1967, Columbia issued several press releases describing the transaction, the invention, and the inventor. In addition, Dr. Grayson Kirk held a press conference in order to publicize the transfer. Columbia was very anxious about adverse publicity resulting from its association with an invention which

Columbia began to perform its obligations under the agreement and hired a manager to work exclusively on the filter. By early August, 1967, sufficient doubts arose about the effectiveness of the filter to cause Columbia to suspend all licensing activities until further tests were conducted. An eniment chemist was engaged by the University to conduct the tests in conjunction with Strickman and certain of his colleagues. Taxpayers, however, became dissatisfied with the progress of the tests and in mid-September gave notice of their intention to terminate the agreement. Formal notice of termination was served in January, 1968, and by February, 1968, the University ceased to have an interest in the filter. (Op. 14-15, App. B, pp. 35a-36a.)

On their 1967 income tax returns, taxpayers claimed charitable contribution deductions as a result of the heretofore described transaction with Columbia University in the following amounts (Op. 14-15, App. B, pp. 35a-36a):

Taxpayers	Amount
Robert S. Raum, et ux.	$ 450,000
Irving I. Rusoff, et ux.	56,500
William W. Suitt, et ux.	978,750
Robert Strickman, et ux.	1,734,300

8/ (continued)
might encourage cigarette smoking. The transfer was characterized in the press release as one designed primarily to aid cancer research as well as the Univeristy. (Op. 14, App. B, p. 35a.)

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

The amounts of these deductions were computed generally by giving a value to the invention (determined by the sale price of certain interests in the invention), and multiplying one half of this figure (the amount claimed as a gift) by the percentage interest allegedly owned by each taxpayer. (Op. 15-16, App. B, pp. 36a-37a.)

The Commissioner of Internal Revenue disallowed the claimed deductions in full on the theory that taxpayers' transfer to the University was a sale, and not a "charitable contribution" within the meaning of Section 170(a) of the Internal Revenue Code of 1954. (Op. 20-21, App. B, pp. 41a-42a.) This determination was sustained by the Tax Court (Op. 20-21, App. B, pp. 41a-42a), and this appeal followed.

SUMMARY OF ARGUMENT

Taxpayers owned rights to a cigarette filter invention. Prior to final development and marketing, they transferred the invention rights by means of an agreement of sale to Columbia University. Under this sale agreement, Columbia was obligated to pay taxpayers percentages of the "net royalties" from licensing ranging from 90 to 49 percent, and to furnish numerous development and marketing services. The Tax Court properly determined that this transfer constituted a sale rather than a charitable contribution because (1) taxpayers received substantial material quid pro quo benefits in exchange for their transfer, and (2) taxpayers had no charitable donative intent.

Section 170(a) of the Internal Revenue Code provides an income tax deduction for a "Charitable Contribution" by way of "contribution or gift." The courts have uniformly held that the statutory deduction is not allowed if there is a substantial relationship between the transfer of money or property and the transferor's receipt of commensurate economic or other material benefits. In other words, no deduction is allowed if the taxpayer receives a substantial material quid pro quo for his purported gift. Even if this requirement is met, however, the deduction is denied if the taxpayer's transfer is not motivated by a subjective donative intent of a charitable character.

1. In the instant case, the documentary instruments used by taxpayers to transfer the invention rights unequivocally effected a sale rather than a charitable gift of the invention rights. The "Assignment Agreement" between taxpayers and Columbia provided for a "sale," in consideration of Columbia's paying taxpayers a share of "net royalties" "as compensation." The agreement obligated Columbia to furnish numerous other services to taxpayers in consideration for the transfer, such as filing patents and conducting patent litigation. The agreement also gave taxpayers an option to revoke the transfer if Columbia's management of the rights was unsatisfactory to taxpayers, and taxpayers in fact exercised this right two months after their transfer. Numerous other documents leading up to this transfer confirmed that the transfer constituted a "sale" for a "purchase price."

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

Taxpayers are legally erroneous in seeking to supersede these operative documents with their testimony that the transaction in substance constituted a charitable donation rather than a sale. This Court has long held that a taxpayer may not for tax purposes disregard the form of a transaction which he has chosen. The operative documents here must be given controlling effect, and as a matter of law effected a sale of the invention rights, with a bargained for quid pro quo.

2. The charitable contribution deduction must alternatively be disallowed because it was not motivated by any subjective donative intent on taxpayer's part. The operative documents discussed above, which evidence and effect a bargained for sale, alone would constitute substantial evidence to support the Tax Court's finding of absence of donative intent.

Moreover, taxpayers have not even challenged the Tax Court's findings, based on substantial evidence, that they transferred the invention rights to Columbia because (1) the University constituted the strong and prestigious organization necessary for dealing with the powerful tocacco companies, (2) it had the credibility and public relations ability needed to market the filter invention, and (3) it had the scientific resources required to further develop the filter. The Tax Court properly inferred that such economic factors motivated the transfer, rather than the charitable donative factors claimed by taxpayers--such as the taxpayer-Strickland's loss of his parents by cancer.

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

3. Taxpayers alternatively contend that if the transfer of the invention rights was a sale rather than a deductible charitable contribution, a partial charitable deduction should be allowed to the extent their invention rights exceeded in value the consideration furnished to them by Columbia. The Tax Court held, however, and taxpayers agree, that no such "bargain sale" charitable contribution is allowable absent a subjective charitable donative intent on their part. Since the Tax Court's finding that taxpayers' had no subjective charitable donative intent is supported by substantial evidence, the Tax Court properly rejected the "bargain sale" contention outright, without making findings as to relative fair market values.

ARGUMENT

THE TAX COURT CORRECTLY CONCLUDED THAT TAXPAYERS' TRANSFER OF INVENTION RIGHTS TO COLUMBIA UNIVERSITY WAS A SALE AND NOT A DEDUCTIBLE CHARITABLE CONTRIBUTION

A. Introduction--A transfer is not a deductible contribution if the transferor receives substantial material quid pro quo benefits, or if he has no donative intent

Section 170 of the Internal Revenue Code of 1954, Appendix A, infra, allows as a deduction any charitable contribution, payment of which is made during the taxable year. Section 170(c)(B) defines a "Charitable Contribution" as a "contribution or gift to or for the use of" a corporation "organized and operated exclusively for * * * charitable * * * or educational" purposes. Not every payment to a qualified corporation is deductible; the

burden of proving that his payment is a "contribution or gift," as those terms have been interpreted for the purposes of Section 170, is on the taxpayer who claims a deduction for the payment.

In Winters v. Commissioner, 468 F. 2d 778, 780-781 (1972), this Court held that taxpayers' payments to an association which operated a school attended by their children did not constitute deductible charitable contributions. The court reasoned that such payments failed to satisfy Section 170 because the taxpayers in fact received an economic benefit therefrom, and they anticipated and expected such a benefit.

The Winters court cited with approval the First Circuit's opinion in Oppewal v. Commissioner, 468 F. 2d 1000 (1972), in which the court amplified somewhat on the relationship between the economic benefit (often called the quid pro quo) test on one hand, and the anticipated or expected benefit test on the other hand. The court made it clear that, even if the taxpayers' subjective motive or intent was charitable, they would be denied the charitable deduction if they received a substantial material quid pro quo for their payment (468 F. 2d, p. 1002):

> We have heretofore expressed our dissatisfaction with such subjective tests as the taxpayer's motives in making a purported charitable contribution. In Crosby Valve & Gage Co. v. C.I.R., 380 F. 2d 146 (1st Cir.), * * * we said:
>
> "While agreeing with the holding of the Tax Court, we think it necessary to register our disagreement with the [Tax Court] majority's emphasis upon a purely charitable motive as a prerequisite for a deductible charitable contribution. Were the deductibility of a contribution under section 170(c)

DEPARTMENT OF JUSTICE
FORM OFFSET COPY FORM

> of the Internal Revenue Code of 1954 to depend on 'detached and disinterested generosity', an important area of tax law would become a mare's nest of uncertainty woven of judicial value judgments irrelevant to eleemosynary reality." 380 F. 2d at 146.

* * *

> The more fundamental objective test is -- however the payment was designated, and whatever motives the taxpayers had in making it, was it, to any substantial extent, offset by the cost of services rendered to taxpayers in the nature of tuition? If so, the payment, to the extent of the offset, should be regarded as tuition for, in substance, it served the same function as tuition.

1. The quid pro quo requirement

Most of the decisions which have interpreted the term "charitable" in Section 170 have emphasized this quid pro quo requirement as determinative, giving much less (or even no) weight, to the subjective, charitable intent requirement. For example, in United States v. Transamerica Corp., 392 F. 2d 522 (C.A. 9, 1968), a taxpayer sought a charitable deduction for the value of a street which it conveyed to the City of Oakland, California (and of the cost of the street's improvement which it paid to the City) to avoid future responsibility and liability for maintenance of the street. The deduction was denied because, it was held (p. 524), the taxpayer "received a direct economic benefit, a quid pro quo" from the City's acceptance of the street which was "apart from any indirect business benefit, such as one incidental to the public use [of the street] or to public recognition of its act of generosity." Accord: Sedam v. United States, 518 F. 2d 242, 245 (C.A. 7, 1975) (no deduction for taxpayer's

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

payment to rest home when "he promised to make the payments to induce the home to admit his mother")[9]; Stubbs v. United States, 428 F. 2d 885 (C.A. 9, 1970) (no deduction for taxpayer's dedication of land for a public way to obtain favorable zoning and additional street frontage for his remaining land); Grinslade v. Commissioner, 59 T.C. 566 (1973) (no deduction where taxpayers received financial and zoning benefits commensurate with the value of the property conveyed by them); Sutton v. Commissioner, 57 T.C. 239 (1971) (no deduction where taxpayer conveyed a right of way to permit commercial development of taxpayer's property); Perlmutter v. Commissioner, 45 T.C. 311 (1965) (no deduction for taxpayer's conveyance of land for public uses to obtain approval of a subdivision plan).

A taxpayer sold sewing machines to schools at a substantial discount and claimed a charitable contribution in the amount of the discount. In Singer Co. v. United States, 449 F. 2d 413 (1971), the Court of Claims found (pp. 423-424) that the discounts were "of a business nature" to increase commercial sales of the taxpayer's machines as girls were trained to use sewing machines and later purchased for their personal use the brand upon which they had received their training. The Court of Claims held (p. 414) that "the benefits to be derived from such [school] discounts were substantial enough to supply the plaintiff with a quid pro quo for the discount which, in turn, effectively

9/ Taxpayers rely on (Br. 23) the District Court opinion in Sedam (74-1 U.S.T.C., par. 9442 (S.D. Ind., 1974)), but failed to note that it was reversed.

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

destroyed the discounts charitable nature." In summarizing the decisions of other courts and expressing the principle which it applied, the Court of Claims stated (p. 423)--

> if the benefits received, or expected to be received, are substantial, and meaning by that, benefits greater than those that inure to the general public from transfers for charitable purposes (which benefits are merely incidental to the transfer), then in such case we feel the transferor has received, or expects to receive, a quid pro quo sufficient to remove the transfer from the realm of deductibility under section 170.

A sufficient benefit to a taxpayer to disqualify a "gift" as a charitable contribution has been described as an economic benefit or as a benefit commensurate with the gift. 10/ "Economic" has been used broadly to include all material benefits, as differentiated from psychological or spiritual benefits, and has not been limited to commercial or financial benefits capable of precise valuation by the market. 11/ However, absolute certainty that there existed the required sufficient relationship between the transfer and the material benefit is not insisted upon in order to disallow the contribution

---

10/ Benefits which are only "incidental" to a gift (not "greater than those that inure to the general public") will not disqualify the gift, Singer, supra (discounts to charitable organizations other than schools); see also Citizens & Southern National Bank of S.C. v. United States, 243 F. Supp. 900 (W.D. S.C., 1965), where the taxpayer's contribution of land for a highway was found to have benefited its property only to the same degree as other property in the vicinity.

11/ In Pettit v. Commissioner, 61 T.C. 634 (1974), a deduction was denied for the value of land dedicated as a public right of way to obtain approval of a subdivision plan by which the taxpayers gave land to their children. The Tax Court held (p. 641) "It is not necessary * * * that the benefit derived from the transfer be an economic benefit. It is enough that the donor has received some benefit beyond the satisfaction which flows from the performance of a generous act."

deduction. It has been suggested that it is enough that a taxpayer avoided difficulty by the gift (Perlmutter v. Commissioner, 45 T.C. 311 (1965)), or that action by a public authority to his benefit was highly unlikely without the gift (Pettit v. Commissioner, 61 T.C. 634 (1974)). A benefit (favorable zoning otherwise uncertain) might have been received without a gift, but the taxpayer made the gift which assured his receipt of the benefit and received no deduction. Stubbs v. United States, 428 F. 2d 885 (C.A. 9, 1970).

2. The charitable or donative intent requirement

On the other hand, a few decisions have emphasized the charitable intent requirement, generally analogizing to the "detached and disinterested generosity" standard set forth for Section 102 gift exclusion purposes in Commissioner v. Duberstein, 363 U.S. 278, 285 (1960). For example, in DeJong v. Commissioner, 309 F. 2d 373 (C.A. 9, 1962), the court held that the individual taxpayers' payments which in reality were for school tuition were not deductible charitable contributions because they were not motivated by taxpayers' subjective detached and disinterested generosity. In United States v. Transamerica Corp., however, the Ninth Circuit explained that this subjective intent test did not eliminate the quid pro quo standard, and opined that the subjective intent test might not be appropriate at all for corporate taxpayers. The Court of Claims has taken a similar position in Singer Co. v. United States, supra, while the First Circuit has indicated that it will give only

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

slight weight to the taxpayer's subjective intent. Oppewal v. Commissioner, supra.

3. The Government's position on the relationship between the Section 170 requirements

In the instant case, while a trust formally effected the transfer, for tax purposes the situation is as if taxpayers individually made the transfer. The Government's position respecting the individual taxpayers' transfers is that the quid pro quo (or other significant relationship) test is the far more important of the two. It may often be the case that a taxpayer may believe, or be willing to testify, that there was no relationship between his payment and his related or resulting receipt of substantial material or tangible benefits; nonetheless, if the objective facts indicate the existence of such a relationship, the deduction must be disallowed. Conversely, however, even if the objective facts indicated that an individual taxpayer received no quid pro quo for his transfer, the charitable deduction would be disallowed if the individual taxpayer did not have the requisite subjective donative intent.

This position is not only logical, but it comports with administrative necessity. If a taxpayer's subjective intent alone were determinative respecting contribution deductions, the Internal Revenue Service would have to conduct a fact-finding proceeding with respect to each taxpayer, no matter how objectively similar was his transfer to that of another taxpayer. Alleged gifts by taxpayers in similar circumstances, for example

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

by the 10 taxpayers here or by the various taxpayers to the schools involved in DeJong, Winters, and Oppewal, might be deductible or not depending on each taxpayer's subjective intent. Obviously Congress did not contemplate such diverse tax treatment, and the resulting administrative burden on the Executive and the Judiciary would be enormous.

4. The standard of appellate review

The standard of appellate review of charitable contribution holdings by lower courts must, of course, depend on which of the two tests is applied. At one end of the spectrum, if documentary and other objective evidence demonstrates the existence of a quid pro quo, then subjective intent cannot be determinative and the issue is purely legal. See In re Beck Industries, Inc., 479 F. 2d 410, 412, fn. 3 (C.A. 2, 1973); Reyher v. Children's Television Workshop, 533 F. 2d 87, 90 (C.A. 2, 1976); Orvis v. Higgins, 180 F. 2d 537, 539-540 (C.A. 2, 1950), cert. denied, 340 U.S. 810 (1950). [12/] At the other end of the spectrum, if taxpayer had undisputedly demonstrated the absence of a quid pro quo, and the testimonial evidence as to subjective intent were disputed, the deduction question would be factual and subject to the clearly erroneous rule. Orvis v. Higgins, supra: Other factual situations falling between these poles would require commensurate variations in the scope of appellate review.

12/ Cf. Biedenharn Realty Co. v. United States, 526 F. 2d 409, 416, fn. 25 (C.A. 5, 1975) (en banc), cert. denied, 45 U.S. Law Week 3249 (Oct. 4, 1976); Turner v. Commissioner, 76-2 U.S.T.C., par. 9660 (C.A. 4, May 6, 1976), reversing in part and remanding, in part, 33 T.C.M. 1167 (1974); Union Planters Nat. Bank of Memphis v. United States, 426 F. 2d 115, 118 (C.A. 6, 1970), cert. denied, 400 U.S. 827 (1970).

See, e.g., Dempster Brothers, Inc. v. Buffalo Metal Container Corp., 352 F. 2d 420, 423 (C.A. 2, 1965).

B. The Tax Court properly concluded that taxpayers' transfer satisfied neither the quid pro quo nor the charitable intent tests under Code Section 170

In the instant case, taxpayers transferred their cigarette filter invention to Columbia University on July 7, 1967. In the same document, Columbia agreed to pay varying percentages of net licensing fees collected ranging to 90 percent "as compensation for the assignment of the Invention", and also to negotiate nonexclusive licenses for use of the invention, to collect licensing fees, to apply for and maintain domestic and foreign patents, and to prosecute and defend the patents. (Op. 12, App. B, p. 33a.) The Tax Court held that taxpayers "expected to receive, directly and indirectly, financial benefits fully commensurate with the value of the property transferred." (Op. 22, App. B, p. 43a.) The court emphasized that "the assignment agreement itself reflects an arrangement for the mutual advantage of the parties, a quid pro quo, not a charitable contribution." (Op. 23, App. B, p. 44a.) In addition, the Tax Court rejected taxpayers' argument that they had a charitable intent for the transfer (Op. 24, App. B, p. 45a), and found that "the theory of a charitable contribution was an afterthought which was not conceived until after the mid-September notice of termination had been sent to Columbia". (Op. 27, App. B, p. 48a.) We submit that the Tax Court was correct as to both requirements.

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

1. The Tax Court correctly disallowed the charitable contribution deduction because the transfer constituted a quid pro quo, bargained for sale of the invention

Taxpayers are in error in placing almost exclusive reliance (Br. 24-32, 35) on numerous expressions of donative intent, thereby also attempting (Br. 33-34) to avoid the sale form of the transaction which they structured. The Tax Court correctly held that taxpayers could not cast aside the sale format which they chose, and that the dispositive documentary instruments unequivocally indicated a bargained for quid pro quo sale of taxpayers' invention.

Most importantly, as the Tax Court concluded (Op. 11-14, App. B, pp. 32a-35a) the terms of the transfer agreement negotiated by taxpayers and Columbia unequivocally provided that the transfer was a sale rather than a gift in the charitable sense. The "Assignment Agreement" itself provided that taxpayers "do hereby sell, assign and transfer unto * * * [Columbia] the full and exclusive right * * * in and to the Invention * * *." (Ex. 25-Y, pp. 4-5 Op. 11, App. B, p. 32a.) The Agreement followed with a long and detailed list of the respective obligations of taxpayers and Columbia under the contract. For example, under Article III, "Payments, Reports, Records and Audit," taxpayers were entitled to receive varying percentages of "net royalties" collected by Columbia, "as compensation for the assignment of the Invention," ranging from

90 percent of the first $5,000,000 to 49 percent of amounts over $25,000,000. (Ex. 25-Y, p. 8; see App. B, p. 33a.)

The Agreement also obligated Columbia to oversee filings of domestic and foreign patent applications (Ex. 25-Y, p. 7); to file foreign patent applications (Ex. 25-Y, p. 5); to negotiate nonexclusive licenses with manufacturers and collect fees prescribed in detail (Ex. 25-Y, pp. 10-11); to prosecute suits for infringement of the patent (Ex. 25-Y, p. 13); to defend suits brought against Columbia resulting from the filter's alleged infringement of other patents (Ex. 25-Y, p. 14); and to refrain from acquiring rights to any other cigarette filter (Ex. 25-Y, p. 12).[13/]

The agreement also contained numerous "Termination" provisions (Ex. 25-Y, pp. 15-18), including those which would allow taxpayers to breach the Agreement if Columbia failed to comply with any provision for a period of 60 days after receipt of written notice thereof (Ex. 25-Y, p. 16), or if annual net royalties did not average at least $100,000 per year for any three consecutive calendar years beginning with 1971 (Ex. 25-Y, p. 15). Article VII permitted taxpayers to assign their interests, but prohibited Columbia from so doing without taxpayers' consent. (Ex. 25-Y, p. 18.)

After thoroughly reviewing this pellucid documentary evidence of sale (Op. 23-25, App. B, pp. 44a-46a), the Tax Court properly

---

13/ Taxpayers totally misconstrue (Br. 39-40) the $55,000 estimate of Columbia's total obligations under the Assignment Agreement. Actually, the $55,000 was solely for one of the several obligations--to hire a business manager and accounting staff for one year. (Ex. AR, p. 4; Ex. AQ, pp. 11-12; Ex. AS, App. B, p. 1a.) The total value of Columbia's services and obligations was never estimated.

held that taxpayers "cannot be heard to disavow the efforts of their attorneys and other representatives acting on their behalf and dismiss these 'formalities' as mere 'lawyers doings'" (Op. 27, App. B, p. 48a). On the basis of this crucial "Assignment Agreement," the Commissioner and the Tax Court were justified in treating the transaction as a sale rather than a charitable contribution. Taxpayers are bound by the sale form which they have chosen, despite the fact that the Commissioner has the option of looking through the form and taxing the substance of a transaction. As this Court explained in Television Industries, Inc. v. Commissioner, 284 F. 2d 323, 325 (1960), in language recently approved by the Supreme Court in Commissioner v. Nat. Alfalfa Dehydrating, 417 U.S. 134, 149 (1974):

> The Commissioner is justified in determining the tax effect of transactions on the basis in which taxpayers have molded them, * * * although he may not always be required to do so * * *. It would be quite intolerable to pyramid the existing complexities of tax law by a rule that the tax shall be that resulting from the form of transaction taxpayers have chosen or from any other form they might have chosen, whichever is less.

Accord, Central Tablet Mfg. Co. v. United States, 417 U.S. 673, 690 (1974).

The rule that the sale form of the Assignment Agreement should be determinative is particularly appropriate here, since the Agreement expressly provides that (Ex. 25-Y, p. 20):

> This instrument embodies the whole agreement among the parties * * * and supersedes any and all prior oral or written negotiations and communications by or on behalf of the parties hereto.

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

Even when a review of the other written documents is made, however--as the Tax Court undertook to do (Op. 7-11, 13, 23, 25-26, App. B, pp. 28a-32a, 34a, 44a, 46a-47a)--it is clear that a sale rather than a gift of the filter invention was effected. At the meetings of April 25 and May 4, 1967, between taxpayers and the Columbia representatives, taxpayers considered and contemplated obtaining capital gains treatment on the sale of the patent, pursuant to Code Section 1235. (Ex. AR, p. 3; Ex. AQ, p. 5; Op. 7, 14, App. B, pp. 28a, 35a.) Such treatment requires a "sale or exchange," which is inconsistent with a charitable contribution.

As the negotiations for sale of the patent proceeded forward, taxpayers' counsel, Robert Katz, wrote Columbia's attorney, John Wheeler, on June 6, 1967, that taxpayers should use a trust to make the transfer, and that (Ex. 18-R, App. B, p. 16a)--

> The Declaration of Trust will give to the Trustees legal title with all of the powers requisite to whatever action may be required in the future as well as the power to sell the patent to Columbia * * * . (Emphasis added.)

Pursuant to this suggestion, taxpayers on June 9, 1967, executed a trust agreement transferring their filter rights to a grantor trust of which taxpayers Robert Strickman and Robert Raum were trustees. As the Tax Court detailed (Op. 9, App. B, p. 30a), this gave the Trust the power "To sell to COLUMBIA * * * the entire right * * * to the INVENTION * * *," and the duty to "collect the net income or proceeds of sale"

(Ex. A, p. 2, App. B, p. 20a). The trust agreement bestowed on the trustees no powers or duties respecting any gift or charitable contribution of the invention.

In the meantime, the Columbia trustees were intensively considering whether to agree to the purchase of the invention rights. In a letter from its counsel to Columbia's president dated June 20, 1967, it was stated that "In your [Dr. Kirk's] covering note to the [Columbia] Trustees you might wish to call their particular attention to * * * the purchase price." (Emphasis added.) (Ex. AS, p. 2, App. B, p. 2a.) The accompanying Proposed Report of the Columbia Committee on Finance to its Trustees summarized taxpayers' "General Proposal" as follows (Ex. AS, App. B, p. 4a; Op. 10, App. B, p. 31a):

> * * * The holders of the invention would assign all of their right, title and interest * * * to the University * * * which would be the sole legal owner, in exchange for a purchase price, specified below, to be paid periodically over a period approximately the life of the patent * * *. (Emphasis added.)

In view of the clear and unequivocal sales terms of the "Assignment Agreement" itself, the Tax Court was legally bound to hold that the transfer constituted a sale rather than a charitable contribution. When the other approximately contemporaneous documents discussed above and in the Tax Court's opinion are considered, the necessity for the sale holding becomes overwhelming.

Taxpayers virtually ignore these dispositive writings, and instead rely almost exclusively on post-transaction testimony of the taxpayers themselves and public relations statements of Columbia as to their intent. As explained above, neither the testimony of taxpayers nor public relations statements of Columbia can override the objective evidence in determining the legal issue whether they received substantial material benefits from the transfer which preclude a charitable contribution deduction. In any event, as the Tax Court found and we shall explain below, these statements and other evidence indicate that it was the subjective intent of taxpayers to sell the invention rights, rather than to make a gift with the requisite subjective charitable donative intent.

2. The Tax Court also correctly disallowed the charitable contribution deduction because the transfer was not motivated by the requisite charitable intent

The Tax Court was not clearly erroneous in finding that taxpayers did not have the requisite subjective charitable donative intent, and could have disallowed the deduction for that reason alone. E.g., DeJong v. Commissioner, supra.[14/]

14/ In Rainier Companies, Inc. v. Commissioner, 61 T.C. 68 (1973), rev'd in unpublished opinion (C.A. 9, Nov. 5, 1975), the Ninth Circuit reversed as clearly erroneous a Tax Court finding that a taxpayer had no charitable donative intent. For unexplained reasons, however, the court of appeals' opinion did not address the quid pro quo issue. It is difficult to see what precedential effect such a disposition can have here.

DEPARTMENT OF JUSTICE
PHOTO OFFSET COPY FORM

Initially, of course, the Tax Court was fully justified in relying on the documents discussed above as indicative of taxpayers' lack of donative intent. Indeed, those portions of the documents referred to above would alone constitute substantial evidence for the court's intent findings. As the Tax Court stated (Op. 26, App. B, p. 47a):

> In the face of cogent documentary evidence, * * * [taxpayers] now repudiate the work of their lawyers as inconsistent with their intentions * * *. We find no merit in these arguments.

Taxpayers have not directly challenged the Tax Court's findings, based on both documentary and testimonial evidence, that (Op. 23, App. B, p. 44a)--

> At the time the assignment agreement with Columbia was negotiated, the filter had been invented but needed testing and refining. Exploitation of the invention was expected to be an expensive and highly speculative venture. The Strickman group was aware of its own lack of credibility, its weakness vis-a-vis the powerful cigarette manufacturers, and the need for further development of the patent. Association with Columbia, a prestigious educational institution with a superior, widely-known medical school, gave the filter valuable favorable purblicity as well as credibility as a cancer deterrent. It also provided the leverage needed for dealing with the tobacco industry in developing a market for the filter. It was with these needs and potential benefits in mind that the Strickman group negotiated the transfer to Columbia. (Emphasis added.)

Moreover, there is ample evidence in support of these findings. Taxpayers first considered commercial corporations to market their product, but favored a strong charity because it would reduce manufacturers' "propensity to cheat," furnish a

"'lily white charisma,'" and give the invention "a lost of 'muscle' through good press and government relations." (Ex. AP, pp. 2-3.) Indeed, taxpayers strongly wished the name "Columbia" to appear on every cigarette package containing the filter. (Ex. AQ, p. 4; see Tr. 35, 134-135.) Cf. Rev. Rul. 63-73, 1963-1 Cum. Bull. 35.[15/] Columbia also satisfied taxpayers' perceived need for a qualified organization which would further develop the invention. (Tr. 126-128, 135; see Ex. 27-Y.)

The Tax Court thus aptly summarized its reasons for finding an absence of charitable intent as follows[16/] (Op. 26, App. B, p. 47a):

15/ Columbia refused this request in order to protect its name. (Ex. AS, App. B, infra, pp. 1a-15a.)

16/ The court's explanation of its reasons for rejecting the charitable motivations so extensively contended for by taxpayers (Br. 8-9, 18, 24-30) needs no elaboration (Op. 27-28, App. B, pp. 48a-49a):

> * * * [Taxpayers] have simply failed to convince us that this transaction had any element of charity. True, both of Strickman's parents died of cancer, and he professed an interest in Columbia's cancer research. Raum testified he was willing to give to Columbia what he anticipated would be millions of dollars because his wife attended some graduate courses there. Suitt's daughter attended Columbia's school of general studies for a limited period of time. Rusoff was aware of Columbia's good work. These motivations are not commensurate with the generosity * * * [taxpayers'] claim, especially when it is remembered that a notice of termination was sent to Columbia during the period the filter was being tested and within less than 3 months after the agreement was signed.

We add only that the alleged charitable motivations of Robert Katz (see Taxpayers' Br. 7-8), who was taxpayers' attorney but not an owner of the invention (see Br. 12-13), are largely irrelevant.

> * * * [Taxpayers] dispute this conclusion, citing testimony that the parties intended in some way to give approximately half their interest to Columbia or that, if there was a sale, it was a bargain sale of the invention to Columbia with a contribution equal to the bargain element. In the face of cogent documentary evidence, * * * [taxpayers] now repudiate the work of their lawyers as inconsistent with their intentions and the substance of the transaction. We find no merit in these arguments.

The post-assignment events confirm that the transaction was a sale rather than a gift. Senate hearings on smoking and cancer were being conducted, and Columbia's tests showed that the filter's efficiency was less than originally thought. (Tr. 167.) As a result, Columbia slowed its development and marketing activities, and in September, 1967, taxpayers promptly gave notice to terminate the assignment. (Tr. 168.) This conduct is scarcely consistent with a charitable intent, and indicates, as the Tax Court found (Op. 27, App. B, p. 48a) that "the theory of a charitable contribution was an afterthought." Moreover, taxpayers have simply misread (Br. 35) the Tax Court opinion in arguing that the Tax Court relied on the presence vel non of an intent to claim a deduction; no such language appears in the opinion below.[17/]

17/ Taxpayers are clearly mistaken (Br. 34) in arguing that the Tax Court erred in allegedly relying on the Senate Hearings Before a Subcommittee of the Committee on Finance on Reviewing Progress Made Toward the Development and Marketing of a Less Hazardous Cigarette, 90th Cong., 1st Sess. Initially, the opinion does not even cite these Hearings; their substance was summarized by a witness at page 167 of the transcript. In any event, the Tax Court would have been justified in judicially noticing these hearings. E.g., United States v. Aluminum Co. of America, 148 F. 2d 416, 445-446 (C.A. 2, 1945) (sitting as court of last resort).

Finally, the Tax Court properly rejected certain references to a "gift" in various public relations statements issued by Columbia and heavily relied on by taxpayers. (Br. 9, 14-15, 18-21, 30.) There was substantial record evidence that these gift references were inserted to make negotiation delays more palatable to taxpayers (Ex. 34), and (in the Tax Court's words (Op. 14, App. B, p. 35a)) to enable Columbia to avoid "adverse publicity resulting from its association with an invention which might encourage cigarette smoking * * * [by characterizing the transfer] as one designed primarily to aid cancer research." See Exs. 27-AO, p. 2; AR, p. 6.

C. The Tax Court correctly held that no part of the value of the invention constituted a charitable contribution under a bargain sale theory

Taxpayers alternatively argue (Br. 38-42) that if the transfer of the filter invention to Columbia University on July 7, 1967, is treated as a sale, then the University received more than it bought and the excess value constituted a bargain sale for which a charitable contribution deduction was allowable.

As taxpayers agree (Br. 39), there are two requirements for a bargain sale charitable contribution deduction: (1) the donee must receive something of value in excess of the "sales price" and (2) there must exist a donative intent respecting the excess at the time of transfer. Grinslade v. Commissioner, 59 T.C. 566, 577 (1973). The issue of valuation in the instant case was not entertained below, because, as the Tax Court found

(Op. 28-29, App. B, pp. 49a-50a), it was not essential to a decision on the merits. As heretofore discussed, the Tax Court correctly found that a donative intent was lacking in every respect as of the date the invention was transferred to Columbia. Accordingly, since one of the two prerequisites for a bargain sale was missing, namely, donative intent, no bargain sale could have taken place. Thus the Tax Court was correct in ruling that a trial of the issue of valuation was unnecessary.

CONCLUSION

For the foregoing reasons, the decision of the Tax Court should be affirmed.

Respectfully submitted,
Myron C. Baum

MYRON C. BAUM,
Acting Assistant Attorney General,

GILBERT E. ANDREWS,
LEONARD J. HENZKE, JR.,
PHILIP I. BRENNAN,
Attorneys,
Tax Division,
Department of Justice,
Washington, D.C. 20530.

DECEMBER, 1976.

CERTIFICATE OF SERVICE

It is hereby certified that service of this brief has been made on opposing counsel by mailing four copies thereof on this 22d day of December, 1976, in an envelope, with postage prepaid, properly addressed to him as follows:

Paul H. Frankel, Esquire
19 Burnt Mill Circle
Oceanport, New Jersey 07757

/s/ Gilbert E. Andrews/cak
GILBERT E. ANDREWS,
Attorney.

7

APPENDIX A

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 170. CHARITABLE, ETC., CONTRIBUTIONS AND GIFTS.

(a) Allowance of Deduction.--

(1) General rule.--There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year. A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary or his delegate.

* * *

(c) [as amended by Sec. 201(a)(1)(B), Tax Reform Act of 1969, P.L. 91-172, 83 Stat. 487] Charitable Contribution Defined.--For purposes of this section, the term 'charitable contribution' means a contribution or gift to or for the use of--

* * *

(2) A corporation, trust, or community chest, fund, or foundation--

* * *

(B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes or for the prevention of cruelty to children or animals;

* * *

BEST COPY AVAILABLE

APPENDIX B

June 20, 1967

Dr. Grayson Kirk, President
202 Low Memorial Library
Columbia University
New York, New York 10027

Re: Strickman Cigarette Filter

Dear Grayson:

At the meeting of the Investments Subcommittee of the Finance Committee held on Tuesday, June 13th, it was suggested that you would wish to advise all of the Trustees with respect to the proposal that the University purchase the Strickman Cigarette Filter.

On further reflection I am inclined to agree with Dan Buttenwieser's comment that the matter is of sufficient importance to justify your distributing the enclosed proposed report of the Committee on Finance dated June 5, 1967, rather than a precis thereof.

I understand that the enclosed proposed report was not adopted by that Committee at its meeting on June 2, 1967, but was instead referred back to its ad hoc Subcommittee, consisting of Messrs. Buttenwieser, Massie and Watt, for further consideration.

That ad hoc Subcommittee, in effect, recommended to the Investments Subcommittee that the matter be pursued further, and

this was agreed to, subject to your polling all of the Trustees as to their acceptance of the proposal in principle, and also subject to the Finance Committee's approval of the proposed Assignment Agreement in final form.

To bring you up to date, after receiving the comments of the interested parties, a revised draft of the Assignment Agreement was prepared, dated June 16, 1967, and is presently receiving the further consideration of the *ad hoc* Subcommittee and of Mr. Strickman and his colleagues. Our patent counsel, Messrs. Fish, Richardson & Neave, have not yet furnished their opinion respecting the patentability of the invention and are awaiting word from the United States Patent Office with respect to the present status of the patent applications.

In the meantime, we are being pressed by Mr. Strickman and his group to go forward on this matter and it would therefore seem desirable to obtain an expression of the Trustees' views as to whether they accept this proposal in principle.

In your covering note to the Trustees you might wish to call their particular attention to ¶(C), the public relations factor, on page 2; ¶(J)(1), the purchase price, at page 5; and ¶(J)(5), Columbia's obligations, at pages 6 and 7.

If the Trustees approve this matter in principle, it is contemplated that the Finance Committee, acting under summer powers, would adopt the enclosed proposed report, with appropriate updating, and adopt the resolutions shown on pages 8 and 9 thereof.

Sincerely,

John W. Wheeler

JWW:MC
CU 570
Enc.
cc:Bloor
Buttenwieser

PROPOSED

REPORT OF THE COMMITTEE ON FINANCE

To the Trustees:

Strickman Cigarette Filter

An ad hoc subcommittee of the Finance Committee, consisting of Messrs. Buttenwieser, Massie and Watt, met with Mr. Robert Strickman, the inventor of an improved cigarette filter, and two of his associates, Mr. Robert Katz and Mr. William Suitt, on May 22, 1967, to discuss the proposed assignment by Mr. Strickman, and his associates, of his cigarette filter invention to the University, in consideration of the University undertaking to explore, through its patent counsel, the patentability of the invention and the strength in offensive litigation of any patent which might issue; to process the pending patent application in the United States Patent Office; to apply for patents in certain foreign countries; to license the invention to tobacco companies at reasonable royalties to be shared, net, by the University and the inventor's group in specified percentages; to prosecute, under the University's control, and to defend, under the University's control, patent litigation; and to expend, in connection with the foregoing, an initial amount of approximately $60,000, all as hereinafter more particularly set forth. Dr. Tapley, of the College of Physicians and Surgeons; Mr. Bloor, the Treasurer; Mr. Wheeler, of general counsel; and Mr. Pugh of patent counsel, were also present at the May 22nd meeting.

We are informed as follows by the ad hoc subcommittee:

(A) The Invention - Mr. Strickman has invented a cigarette filter which succeeds in reducing tar and nicotine appreciably more than present filters do. Its second distinguishing feature is that, unlike present filters, smokers may distinguish brand flavors when using the Strickman filter. A third distinguishing characteristic of the Strickman filter is that there is no drying action as there is with present filters. The substance of the invention is an inorganic-organic polymer (which is defined in Webster's New Collegiate Dictionary as: Any of two or more polymeric* compounds; one of higher molecular weight, especially one produced by polymerization**.) There is allegedly no toxicity in the filter material. While it is known that the Strickman filter will remove substantial amounts of tar and nicotine, as indicated above, according to Dr. Tapley, no one is sure (and probably won't be for 15 to 20 years)

*Consisting of the same elements in the same proportion by weight but differing in molecular weight, as cyanic acid and cyanuric acid.

**To change (by union of two or more molecules of the same kind) into another compound having the same elements in the same proportions, but a higher molecular weight and different physical properties.

Report of Committee on Finance

Strickman Cigarette Filter

that tar and nicotine are the carcinogenic "villians" and that there are not other carcinogenic agents in the tobacco which are not being filtered out by any known filter.

(B) General Proposal - The holders of the invention would assign all of their right, title and interest in the patent application to the University (or to a subsidiary corporation) which would be the sole legal owner, in exchange for a purchase price, specified below, to be paid periodically over a period approximating the life of the patent, which payments would be contingent on the amount of royalties received from the University's licensees, and in consideration of the University undertaking certain obligations outlined below.

(C) Public Relations Factor - The ad hoc subcommittee and the Committee on Finance are concerned about the public relations factor necessarily present in the University's involvement in this matter. If this project is to be undertaken, then the University's position must be that, since it has been conclusively demonstrated that people will smoke cigarettes despite the health hazard warnings already issued with respect to cigarette smoking, then it is preferable that they smoke with a good filter. This factor will dictate the charging of reasonable royalties on a non-exclusive basis, as hereinafter appears. This factor will also require that the University's name not appear in any trademark to be issued and that the University have complete control over any patent litigation in which it might be engaged, as hereinafter appears. This factor will also cause the University to avoid the ownership of any other cigarette filter, as hereinafter appears. The public relations factor can be minimized, but not eliminated, through the use of University Patents Inc. or some other subsidiary corporation owned or controlled by the University. The possible use of this alternative is provided for, as hereinafter appears.

(D) The Licensing Prospects - With the use of this filter, the tobacco industry might be able to take its legally required "caution notice" off the cigarette package. This would make every major tobacco company most anxious to acquire a license and the royalties under the license would be expected to be substantial. Even a cure for cancer would not prevent its recurrence and therefore the need for the filter would not diminish. According to the Surgeon General's report,

unfiltered tobacco is also a major cause of emphysema and cardiovascular disease. Report of Committee on Finance

(E) Tests - Tests have been conducted by Fitelson Laboratories, Inc. on May 2, 9 and 15, 1967. Copies of the reports of analysis of those dates are attached. Only informal taste tests have been made, using individuals at random, and no further taste-testing is contemplated at this time. The University will seek to obtain further assurances that the filter itself contains no toxic elements. A copy of a qualified report of Charles J. Umberger, Ph.D., Director of Laboratories, Office of the Chief Medical Examiner, City of New York, dated May 22, 1967, is also attached. Strickman Cigarette Filter

(F) Patent Status of the Invention -

(1) United States - Mr. Strickman filed a patent application in 1960, which is pending, and which has been amended twice, in 1966 and 1967. The University's patent counsel, Harry R. Pugh, Esq., of Messrs. Fish, Richardson & Neave, will give his opinion on the patentability of the invention and its probable chances of survival in offensive litigation, if challenged. Mr. Pugh will engage a Washington attorney to conduct a patent search for earlier claims in the cigarette filter field. Mr. Pugh estimates that the search might take from one to three months to accomplish.

(2) Foreign - It will not be necessary, for the purposes of Mr. Pugh's opinion, to make a foreign patent search at this time. For future plans as to foreign patents, see below.

(G) Disclosure of Confidential Information for the Purpose of University Patent Counsel's Opinion - An appropriate disclosure letter has been written by Mr. Strickman to the University providing for furnishing to Mr. Pugh copies of all patent application papers. For the time being, disclosure of the invention has been made only to Mr. Pugh, certain of his partners and associates, and to the Washington patent attorney chosen by him for the purpose of making a search. At this stage of the matter, no disclosure has to be made to chemists or to filter manufacturers. The opinion which Mr. Pugh's firm will render to the University will cover the probable patentability and worth of the patent applications and will include his firm's appraisal of what the issued patent's chances would be in offensive

litigation. Mr. Pugh does not consider it necessary at this time to search for chemical patent claims which may have been made which would encompass the chemical composition of the Strickman filter. Mr. Strickman and his patent attorney, Mr. Nydick, will furnish such information as Mr. Pugh may require to enable him to render his opinion.

Report of Committee on Finance

Strickman Cigarette Filter

(H) The Inventor and the Other Holders of the Invention - In addition to Mr. Strickman, whose efforts alone created the invention, there are a number of other individuals who own the invention, some of whom have acquired an interest in the invention in exchange for consideration in money or money's worth paid to the creator, Mr. Strickman, prior to actual reduction to practice of the invention, and some of whom are neither the employer of the creator nor related to him, so that the income received by them from the invention would qualify for capital gains treatment under §1235 of the Internal Revenue Code. A "declaration of trust", being prepared, will disclose who are the "holders of the invention" and their relative interests therein and will contain a power of attorney to Mr. Strickman to represent them as assignor in dealings with the University and its licensees. The corporation of which Mr. Strickman is president, Allied Testing and Research Laboratory, is an ordinary business corporation, organized under the laws of New Jersey, having eight stockholders owning approximately 49% of the stock, with Mr. Strickman owning the balance of approximately 51% of the stock. Allied is only about six months old and has no shop rights in his invention and owns a 1% interest in it. Mr. Strickman created the invention in his own laboratory.

(I) Tax Status - Columbia - The University is generally free of federal income taxation pursuant to §501(c)(3) of the Internal Revenue Code as a corporation organized and operated exclusively for educational purposes. "Unrelated business income" of charitable corporations is taxed under §511 et seq. of the Internal Revenue Code, but §512(b)(2) excludes from unrelated taxable business income royalties on patents. If the patent is assigned to a wholly owned subsidiary of Columbia and if such subsidiary performs no functions other than the collection of royalties on the patent and the payment of those royalties to Columbia, then the subsidiary will be exempt from tax under §501(c)(2) of the Internal Revenue Code. The various consultants

Report of Committee on Finance

Strickman Cigarette Filter

and business managers (mentioned below) should be hired by and work for Columbia and not the subsidiary corporation. If such persons are employed by the subsidiary, that corporation may be taxable as an ordinary business corporation. It is not believed that the proposed transaction is vulnerable to a charge that an improper benefit is being derived from Columbia's tax-exempt status, although no one has yet sought to appraise the reasonableness of the price which the University will pay (in terms of royalty sharing) for the patent. No adverse tax consequences under the present law are foreseen, even if the claim is made that Columbia is "selling" the use of its name. In any event, as hereinafter appears, Columbia's name will not be included in the "trademark" or, except at its option, in patent litigation.

(J) Assignment - An assignment agreement between the inventor and the holders, as assignors, and the University, as assignee, will, in addition to the usual provisions, cover the following points of a business nature, none of which has yet been fully negotiated between the inventor's group and the University:

(1) Purchase Price - The net royalties would be divided as follows:

Out of	Columbia would receive	Holders would receive
First $5 million	10%	90%
Second $5 million	20%	80%
Third $5 million	30%	70%
Fourth $5 million	40%	60%
Fifth $5 million	50%	50%
Above $25 million	51%	49%

Out of the first $25 million of net royalties, Columbia would receive $7.5 million and the holders would receive $17.5 million. The $25 million plateau was suggested by the inventor's group on the basis of current sales volume, filter use, and the probable use of the Strickman filter. This figure was arrived at on the following basis: 2.8 billion cartons of cigarettes are sold in the United States annually: approximately 70% of these, or approximately 2 billion cartons, are filter cigarettes; and approximately 40% of the filtered cigarettes would use the Strickman filter; making a total of eight hundred million cartons per year of Strickman filter cigarettes to be sold, which, at three cents

per carton, would produce approximately $25 million per year in gross royalties. Thus the inventor's group expect that this plateau figure would be reached within a year.

Report of Committee on Finance

Strickman Cigarette Filter

(2) Royalties to be Charged Licensees -

(a) Fixed Royalties - As noted above, the assignors suggest that the royalty rate should be three cents per carton sold with the Strickman filter. The public relations factor enters into this provision. The Strickman filter must be generally available to the entire tobacco industry. The royalty must therefore be reasonable. In that connection, the cigarette manufacturers sell filter cigarettes to wholesalers at approximately $1.80 per carton. Of this amount, 80 cents is payable as Federal Excise Tax. Accordingly, the gross selling price per carton, net of Excise Tax, is $1.00. It is therefore proposed, as indicated above, that the royalty be fixed at 3 cents per carton, or 3% of $1.00, the gross selling price per carton. The advertising budget in the tobacco industry is much higher than the proposed royalties. The tobacco industry presently fears that state legislation will literally tax cigarettes out of existence unless the health threat problem is solved through an adequate filter. The expense of producing the Strickman filter is substantially equivalent to the cost of filters presently in use. There is no foreseeable limit on the supply of materials needed to produce the Strickman filter. The problem in maintaining a high royalty level will be obtaining a "tight license" which would protect against each licensee's claim that it now had produced "the SUPER-Strickman Filter" or its own better quality filter.

(b) Minimum Royalties - The assignment agreement will provide that the license agreement will prescribe minimum royalties, minimum advance royalties and minimum annual royalties to be paid by the licensees, in amounts to be agreed upon in advance.

(3) Non-exclusivity of Licenses - The public relations factor also enters into this provision.

BEST COPY AVAILABLE

Report of Committee on Finance

The filter must therefore be made available to the entire tobacco industry on a non-exclusive basis.

Strickman Cigarette Filter

(4) Trademark - Again, the public relations factor is involved. The filter will be called "the Strickman Filter" or by some other name not including "Columbia". The cigarette packages will not bear Columbia's name as licensee of the filter.

(5) Columbia's Obligations -

(a) The University will be obliged to expend money for the expenses incurred in satisfying itself that the Strickman patent is patentable and in prosecuting the Strickman patent application.

(b) The University will be obliged to expend money for foreign market protection, at least in Western Europe, including the United Kingdom. The expense of filing foreign patent applications would cost several thousand dollars and there would also be annual taxes on the foreign patents to keep them in effect.

(c) Some of the net royalties received by the University would have to be used for medical research.

(d) The University will agree not to license any other patent for a cigarette filter to the tobacco industry, to the extent permitted by law. This provision also raises the public relations factor, for the University would not wish to have it said that it was withholding from the public an even better filter than the Strickman filter in order to protect its royalties under licenses of the Strickman filter. This problem could be avoided, however, by the University not accepting ownership of any other cigarette filter.

(e) The University will be able to assign th tent to any corporation owned or controlled by it, but not otherwise, and would re liable for such subsidiary's obligations. Thus, an initial or further assignment t versity Laboratories Inc. would be permitted. The University might also sub-contract of its obligations to Research Corporation.

Report of Committee on Finance

Strickman Cigarette Filter

(f) The University would hire Mr. Strickman as a consultant upon terms to be agreed.

(g) The University would hire Mr. Suitt as marketing consultant upon terms to be agreed.

(h) The University would hire a business manager and accounting staff at a cost of approximately $55,000 per year. This work might possibly be sub-contracted, in whole or in part, to Research Corporation.

(i) The University would be diligent in prosecuting United States and foreign patent applications, at the University's expense, covering improvements. Although the University would use its own patent counsel in prosecuting applications for improvements, Mr. Strickman's own patent counsel, Mr. Nydick, will be consulted.

(j) The University would be diligent in licensing the patent to cigarette manufacturers.

(k) The University would be diligent in defending the patent in defensive litigation. Although the naming of the University as a party defendant would affect its public relations, Mr. Pugh advises that the suits by rival patent claimants are against the makers and users of the patent, and not against the owner of the patent.

(l) The University would be diligent in prosecuting infringers of the patent in offensive litigation. Since the institution of such litigation in the name of the University involves a public relations factor, the University will insist upon sole control of the litigation, or, in the alternative, to minimize the problem, will insist that such suits be prosecuted in the name of others, including, perhaps, one of the University's subsidiary corporations

If it is the decision of the Trustees to proceed in this matter as outlined above, then, in order to permit the University (acting by its Clerk, or his substitute, and

its Treasurer, or his substitute, with the advice of counsel and with the concurrence of the Committee on Finance) to enter into an appropriate agreement with the inventor of the Strickman cigarette filter and his associates prior to the next meeting of the Trustees on October 2, 1967, which agreement would, among other things, cover the subjects outlined above, we recommend the adoption of the following resolutions: Report of Committee on Finance; Strickman Cigarette Filter

RESOLVED, That the Clerk or, in his absence, the Associate Clerk, and the Treasurer or, in his absence, the Assistant Treasurer, of the University, hereby are authorized (acting with the advice of counsel and with the concurrence of the Committee on Finance) to enter into an appropriate agreement, substantially on the terms outlined in the Report of the Committee on Finance, dated June 5, 1967, with Robert Strickman, and others, providing for the purchase by the University of the cigarette filter owned by the said Robert Strickman in consideration of the obligations undertaken by the University therein, with such modifications and refinements thereof as may hereafter be approved by said officers, acting with such advice and concurrence; and be it further

RESOLVED, That said officers be and they hereby are similarly authorized and directed to expend out of the general funds of the University such sums as shall be reasonably necessary to carry into effect the foregoing resolution; and be it further

RESOLVED, That the general funds account of the University shall be reimbursed for the foregoing expenditures out of the gross royalties hereafter received by the University from the licensees of the patent rights to the aforesaid invention; and be it further

RESOLVED, That said officers be and they hereby are similarly authorized to make, execute and deliver such other and additional documents, including but not limited to, license agreements, and to take such further action as may be necessary or appropriate to carry into effect the foregoing resolutions, including, but not limited to, the use of University Patents, Inc., or any other subsidiary corporation, owned or

controlled by the University, to carry into effect the foregoing resolutions, and the guaranty by the University of the undertakings of any such subsidiary corporation in connection therewith.

Report of Committee on Finance

Strickman Cigarette Filter

Respectfully submitted

/Not signed/

Percy Uris, Chairman
Robert W. Watt, Vice Chairman
Alan H. Temple
Frederick R. Kappel
William E. Petersen
Lawrence A. Wien

CONSULTATION AND ANALYSIS
LABELING AND SANITARY CO

OFFICIAL LABORATORY OF
NEW YORK PRESERVERS ASSN.

FITELSON LABORATORIES, INC.
CONSULTING AND ANALYTICAL CHEMISTS
254 WEST 31ST STREET
NEW YORK, N. Y. 10001
TEL. CHELSEA 3-0703

17493 May 2, 1967

REPORT OF ANALYSIS.

FOR: Dr. Donald Tapley
Department of Medicine, Columbia University
630 W. 168 Street, New York 32, N.Y.

PRODUCT: Lucky Strike Filter Cigarettes; Special Cigarettes.

SAMPLE IDENTITY:
Special cigarettes stated to be Lucky Strike with special filters

ANALYSIS:

Four cigarettes smoked in standard smoking apparatus with smoke caught in a Cambridge Filter. Total Particulate Matter (T.P.M.) obtained and then Nicotine determined in this material. Note that T.P.M. contains about 12% moisture from the smoke.

	Av. No. Puffs	T. P. M. mg. / cig.	Nicotine mg. / cig.
Lucky Strike, special	9.75	4.4	0.23
Lucky Strike, filter (control)	9.5	19.7	1.04

COMMENT:

J. Fitelson, Ph. D.
Director.

BEST COPY AVAILABLE

FITELSON LABORATORIES, INC.
CONSULTING AND ANALYTICAL CHEMISTS
254 WEST 31ST STREET
NEW YORK 1, N. Y.
TEL. OXFORD 5-0703

#17559(a) May 9, 1967

REPORT OF ANALYSIS

FOR: Dr. Donald Tapley
Columbia University
Department of Medicine
630 W. 168 Street
New York, N.Y. 10032

PRODUCT: Cigarettes (Filter)

SAMPLES: Various commercial filter cigarettes and special filter cigarettes as noted below

ANALYSIS: Cigarettes smoked in standard smoking apparatus and smoke caught in Cambridge Filter for weighing as total particulate matter.

Cigarette		Av. No. Puffs	Total Particulate Matter mg./ cigarette
Camel, Filter, King.			
Commercial	filter	9.25	22.5
Special	"	9.5	8.6
Marvel, Filter, King			
Commercial	"	7.0	8.6
Special	"	7.0	3.7
Kent, King.			
Commercial	"	8.0	18.5
Special	"	8.75	5.2
Winston, Filter, 100 mm.			
Commercial	"	11.3	26.2
Special	"	11.7	12.3
Marlboro, King.			
Commercial	"	7.5	20.3
Special	"	7.75	9.3
L & M, King			
Commercial	"	8.25	20.9
Special	"	9.0	6.9
Lark, King			
Commercial	"	8.0	20.1
Special	"	8.0	9.2
True, King Special	"	8.0	7.9
Viceroy, King, Special	"	8.25	5.8
" " "	"		
(tighter pack)		8.5	3.8
Lucky Strike Filter, Special		8.0	4.5

Note: Nicotine analyses on above T.P.M. will follow.

J. Fitelson, Ph.D.
Director.

FITELSON LABORATORIES, INC.
CONSULTING AND ANALYTICAL CHEMISTS
254 WEST 31ST STREET
NEW YORK 1, N. Y.
TEL. OXFORD 5-0703

#27559(b) May 25, 1967

REPORT OF ANALYSIS

FOR: Dr. Donald Tapley
Columbia University
Department of Medicine
630 W. 168 Street
New York, N.Y. 10032

PRODUCT: Filter Cigarettes

SAMPLES: Various commercial filter cigarettes; Special filter cigarettes ; as noted below

ANALYSIS: Cigarettes smoked in standard smoking apparatus, smoke caught in Cambridge filter and total particulate matter weighed. Cambridge filter then analyzed for Nicotine

Cigarette	Nicotine mg. / cigarette
Camel, Filter, King.	
Commercial filter	1.14
Special "	0.42
Marvel, Filter, King	
Commercial filter	0.25
Special "	0.13
Kent, King	
Commercial "	0.95
Special "	0.24
Winston, 100 mm.	
Commercial "	1.17
Special "	0.52
Marlboro, King	
Commercial "	1.12
Special "	0.45
L & M, King	
Commercial "	1.02
Special "	0.30
Lark, King	
Commercial "	1.00
Special "	0.39
Kool, King, Special Filter	0.95
Viceroy King, Special Filter (a)	Not tested for Nicotine
Special Filter (b)	" " " "
Unity Menthol, Special Filter	" " " "

J. Fitelson, M.D.
Director.

ROBERT A. KATZ
ATTORNEY AT LAW
375 PARK AVENUE
NEW YORK, NEW YORK 10022

572-7271
AREA CODE 212

June 6, 1967

John Wheeler, Esq.
Thacher Proffitt Prizer Crawley & Wood
40 Wall Street
New York, New York

Dear Mr. Wheeler:

I have carefully reviewed the Assignment Agreement which you have drawn and have taken the liberty of making a small number of proposed revisions which I submit herewith for your consideration in the form of a photocopy of a mark-up copy of your draft. Although the Strickman group has not yet met to discuss in detail the [illegible]ment and my proposed changes, I can assure you that it generally reflects the agreement of the parties. I would like to explain my reasons for some of the changes and also to highlight some of the problems that still remain to be solved, as follows:

1. In view of the fact that the Strickman group must, under certain circumstances, act in concert pursuant to the agreement, I have recast the Agreement as one between Columbia University on the one hand and Messrs. Strickman and Raum on the other hand as Trustees under a Declaration of Trust for the benefit of all of the members of the Strickman group who are too numerous to operate in concert quickly and effectively. The Declaration of Trust will give to the Trustees legal title with all of the powers requisite to whatever action may be required in the future as well as the power to sell the patent to Columbia University pursuant to the Agreement.

I have not included in the Agreement any provision for payment other than to the Trustees. It may be useful at some future time to provide for payment directly to the beneficiaries of the Trust. I am sure that at that time this minor detail can be handled with relative ease.

2. The draft agreement refers the matter of pricing to the tobacco industry back to the assignors. Without regard to the tax implications resulting from this reference, I think that as a practical matter Columbia should have the power to set the price and other terms in any license, subject only to pre-arranged limitations to be set forth in the agreement between Columbia and the Strickman group. I have therefore revised paragraph 2.18 to provide for minimum pricing arrangements. In this connection, I think also that paragraph 2.4 must necessarily be subservient to the provisions of paragraph 2.18.

DKT NO. 62-Rad(R)
EXH. 16-R

BEST COPY AVAILABLE

 June 6, 1967

3. The matter of execution of applications for issuance and re-issuance of patents by the assignors should, I think, be covered with Mr. Pugh to deal with the eventuality of the death or incapacity of Mr. Strickman prior to termination of the Agreement.

4. The obligation expressed in paragraph 2.10 is, of course, principally that of Mr. Strickman. Conceivably it might be desirable to spell this out.

5. Paragraph 2.11 dealing with the division of net royalties is expressed in U.S. dollars. There are, of course, problems with foreign currencies generally and with blocked currencies in particular. I suggest that we deal with these by separate agreement if, as and when foreign licenses are imminent.

6. I have added four countries in paragraph 2.14 and suggest that Mr. Pugh or Mr. Strickman's patent counsel may be able to suggest additional inclusions or deletions from the existing list. In paragraphs 2.26 and 2.12 I have made date and period changes for your consideration.

7. In the event that we do utilize a Declaration of Trust, paragraph 2.31 will become surplusage in its present form. I suggest that we may wish to provide language permitting unrestricted assignment of beneficiary interests in the Trust Estate.

Messrs. Raum, Strickman, Suitt and I are meeting on this and other matters on Thursday afternoon at 3:00 p.m. at Mr. Raum's office. If you have an opportunity to review the enclosure prior to that meeting, possibly we may be able to settle, as between you and me at least, prior to the meeting some of the small issues which remain outstanding at this time. At the Thursday meeting with Messrs. Raum, Strickman and Suitt, I hope that we shall be able to determine with respect to all of the issues the position of the Strickman group.

I expect to be out of the Country all of next week; Monday and Tuesday in Canada and the balance of the week in Germany, or perhaps in Germany and Spain. It would be extremely helpful, therefore, if we can bring this matter at least to an informal conclusion by the end of this week so that only re-typing remains to be done next week, and execution and exchange of agreements can be had promptly.

I have not suggested in my comments above that the Agreement be conditional upon the favorable report of Mr. Pugh on the assumption that by the time we are all prepared to sign it, Mr. Pugh will have completed at least his patentability search with respect to the invention. I assume, of course, that the results of Mr. Pugh's infringement search are not germane to execution of this Agreement and, in fact, will have application only to vending by licensees which cannot, under the circumstances, take place prior to completion of Mr. Pugh's infringement search.

John Wheeler, Esq. --- 3 June 6, 1967

Mr. Raum has just telephoned me to suggest that paragraph 2.3 be revised to provide that the expense of foreign patent applications shall be on the assignee in the first instance and that the covenant against disclosure contained in paragraph 2.23 be applicable to the assignee as well as to the assignors.

Sincerely,

Robert A. Katz

RAK:cj
Enc.

cc's: Robert S. Raum, Esq.
Mr. Robert Steichman
Mr. William Suitt

TRUST AGREEMENT

TRUST AGREEMENT made June 9, 1967 between the undersigned, as Grantors, and ROBERT L. STRICKMAN and ROBERT S. RAUM, as Co-Trustees.

TRUST PROPERTY

The Grantors hereby transfer to the Trustees all of their right, title and interest to the INVENTION for a cigarette filter for which a Patent Application No. 59035 has been filed with the United States Patent Office bearing date September 28, 1960 and any and all improvements thereto, hereinafter termed the trust property, in trust, for the purposes and on the conditions hereinafter stated.

The Grantors individually and jointly represent that they have not heretofore transferred any interest to said INVENTION and that they collectively own one hundred (100%) per cent of the right, title and interest to said INVENTION, and by this instrument they hereby transfer to the Trustees the entire right, title and interest in and to said INVENTION free and clear of any liens, encumbrances or claims of others.

DISPOSITIVE PROVISIONS

The Trustees shall hold, manage and invest the trust property, and shall collect and receive the income thereon, and after deducting all necessary expenses incident to the administration of the trust, shall dispose of the principal and income of the trust as follows:

1. The Trustees shall collect the net income or proceeds of of sale and shall make distribution thereof upon receipt to the Grantors in accordance with the percentages appearing alongside their signatures or to their assignees in accordance with any

EXH. A

DKT NO. 602-72 dd
pl. 19=5

writing dated subsequent hereto.

2. The Trustees shall distribute and pay over the corpus to the then beneficiaries of the trust twenty-one (21) years after the death of the survivor of the Grantors and thereupon the trust shall terminate.

TRUSTEES' POWERS

1. To sell to COLUMBIA UNIVERSITY or to any of its designees the entire right, title and interest in and to the INVENTION upon such terms as in their sole discretion and judgment may be deemed for the best interest of the beneficiaries hereunder.

2. To compromise, settle, arbitrate or defend any claim or demand in favor of or against the trust and to enter upon such contracts and agreements and to make such compromises or settlements of debts, claims or controversies as they may in their sole discretion deem necessary or advisable.

3. To incur and pay the ordinary and necessary expenses of administration, including (but not by way of limitation) reasonable attorneys' fees, accountants' fees, and the like.

4. To act hereunder through an agent or attorney-in-fact, by and under power of attorney duly executed by the Trustees, in carrying out any of the powers and duties herein authorized.

SUCCESSOR TRUSTEES

It is intended that there be two (2) Trustees acting at all times. In the event that any Trustee shall be unable or unwilling to act in said capacity, the beneficiaries under this TRUST AGREEMENT shall appoint by vote of a majority in interest the successor Trustee to act in his place. Any successor Trustee shall have all the duties and powers assumed and conferred in this agreement upon the Trustees.

SITUS

This trust has been executed and delivered in the State of New York and shall be construed and administered according to the laws of that State.

IN WITNESS WHEREOF, the Grantors and the Co-Trustees have hereunto executed this Agreement.

Robert L. Straßmann, Co-Trustee

Robert S. Raum, Co-Trustee

GRANTORS:

65 T. C. No. 41

UNITED STATES TAX COURT

IRVING I. RUSOFF and PERLE P. RUSOFF, et al., 1/ Petitioners v. COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket Nos. 682-72, 1358-72, 1724-72, 2212-72, 3740-72.

Filed December 2, 1975.

Petitioners and others owned a cigarette filter invention which they transferred to a trust created in June 1967, retaining the right to the trust's income as well as any gains from the sale of its corpus. In July 1967, the trust transferred the invention to Columbia University under an agreement obligating the university, among other things, to

---

1/ The following cases are consolidated herewith: Robert Strickman and Rose Strickman, docket No. 1358-72; William W. Suitt and Kathryn S. Suitt, docket No. 1724-72; Robert S. Raum and Ruth Raum, docket No. 2212-72; Irving Rusoff and Perle Rusoff, docket No. 3740-72.

SERVED DEC 2 1975

prosecute domestic and foreign patents, protect them from infringement, and negotiate and enter into licensing agreements with the cigarette industry. Petitioners reserved for themselves a substantial percentage of any royalties earned under the licensing arrangements. Because the university did not carry out its obligations under the agreement in a manner satisfactory to petitioners, in Sept. 1967 the trust gave notice of intention to terminate the agreement and completed the termination procedures in Feb. 1968. Petitioners claimed charitable contribution deductions on their 1967 income tax returns for one-half of the alleged value of the invention transferred to the university.

Held, since the trust created by petitioners, to which they transferred the invention, was a "grantor" trust within the provisions of sec. 677, I.R.C. of 1954, sec. 671, I.R.C. of 1954, entitles petitioners to their proportionate share of deductions for any charitable contributions by the trust.

Held further, however, the transaction with Columbia was not a charitable contribution within the meaning of sec. 170, I.R.C. of 1954.

Paul H. Frankel, for the petitioners.

Curtis W. Berner and Peter Matwiczyk, for the respondent.

FEATHERSTON, Judge: Respondent determined the following deficiencies in income tax in these consolidated cases:

Docket No.	Year	Deficiency
682-72	1967	$1,184.97
1358-72 1/	1967	4,830.03
	1968	7,460.42
1724-72 1/	1967	1,026.39
	1968	5,592.23
	1969	815.00
2212-72	1967	3,887.00
	1968	6,059.00
	1969	7,1[illegible]9.00
3740-72	1968	1,999.60

1/ In an amendment to his answer, respondent alleged additional deficiencies for 1968 in docket Nos. 1358-72 and 1724-72 in the amounts of $25,499.09 and $17,344.98, respectively. These allegations, as well as certain other issues, are not presented for decision in this proceeding.

Other issues having been severed, the following are presented for decision in this proceeding:

1. Whether petitioners owned any interest in an invention at the time it was transferred to Columbia University; and

2. Whether the transfer of the invention to Columbia University constituted a charitable contribution within the meaning of section 170. 2/

2/ All section references are to the Internal Revenue Code of 1954, as in effect during the tax years in issue, unless otherwise noted.

FINDINGS OF FACT

Petitioners Irving I. Rusoff (hereinafter Rusoff) and Perle P. Rusoff, husband and wife, were legal residents of Park Ridge, New Jersey, at the time their petitions were filed. Petitioners Robert S. Raum (hereinafter Raum) and Ruth Raum (now deceased) were husband and wife and legal residents of New York, New York, at the time their petition was filed. Petitioners William W. Suitt (hereinafter Suitt) and Kathryn S. Suitt, husband and wife, were legal residents of Greenwich, Connecticut, at the time their petition was filed. Petitioners Robert Strickman (hereinafter Strickman) and Rose Strickman, husband and wife, were legal residents of Rivervale, New Jersey, at the time their petition was filed.

In the late 1950's, Strickman began the development of a cigarette filter which would reduce particulate matter (tars) and nicotine gas from cigarette smoke without altering the natural flavor of the tobacco. He was motivated in part by the fact that both of his parents had died of cancer. His efforts produced the Strickman Cigarette Filter (hereinafter "filter" or "invention") which it was believed would appreciably reduce the level

of inhaled tar and nicotine below the levels then attained by conventional filters. An application for a patent was filed on September 28, 1960, and continuations of that application were filed on January 11, 1965, December 6, 1966, and April 11, 1968. On November 9, 1971, United States Patent 3,618,618 was granted for the filter.

While he was in the process of developing the filter, Strickman transferred undivided percentage interests in it to various individuals, including Raum, Suitt, and Rusoff. The transfers were made by informal oral or written assignments and were not evidenced by any documents in the customary legal form. The transfers were either compensation for assistance in developing the filter or, in some cases, merely gifts.

Suitt received his interest in the filter in 1966. He had some knowledge of the cigarette industry, and he thought the filter had significant economic potential. In early 1967, Suitt consulted Robert Katz (hereinafter Katz), an attorney, and introduced him to Strickman. In Strickman's laboratory, Katz observed tests of several sample filters, perused test results comparing the effectiveness of the filter with conventional filters, and concluded that the economic potential of the filter was

"astronomical." He recommended that the rights to the filter be transferred to an organization which would be more capable than they in dealing with the powerful tobacco manufacturers. Such an organization, he advised, could more effectively negotiate licensing agreements with the tobacco industry.

Katz suggested that the transfer be made to the Medical School of Columbia University (hereinafter Columbia, the university, or the medical school). Several doctors associated with that institution lived in Katz's community, and some of them had been instrumental in saving the life of Katz's son several years earlier. Katz's contacts would facilitate Columbia's acceptance of the transfer. Columbia was thus readily and quickly available as a desirable transferee, and it had the facilities to further develop the filter.

Since the other owners of interests in the filter had no objection to an arrangement with Columbia, negotiations with Columbia regarding the transfer were initiated. Katz, who represented the owners of the filter (hereinafter referred to as the Strickman group), informed Dr. Donald Tapley, a neighbor and faculty member of the medical school, about the filter and the desire of its

owners to transfer it to Columbia. Dr. Tapley contacted William Bloor, treasurer of Columbia, who initiated proceedings within the university necessary for a transfer of the filter. On April 25, 1967, and May 4, 1967, meetings were held between representatives of the Strickman group and Columbia. Attending these meetings on behalf of the Strickman group were Strickman, Suitt, and Katz. Raum attended only the meeting held on April 25, 1967.

The participants at these meetings discussed the nature of the invention; the patent status of the invention; the tax considerations for the owners of interests in the filter; 3/ the nature of possible licensing arrangements between Columbia and the cigarette manufacturers, including royalty charges; proposed provisions of an assignment agreement between the Strickman group and Columbia, including amounts referred to as a "purchase price to be paid periodically * * * which payments would be contingent on the amount of royalties

---

3/ At the April 25, 1967, meeting, the applicability of sec. 1235 was discussed. That section, if applicable, would recognize payments received by the Strickman group as gain from the sale or exchange of a capital asset.

received from the University's licensees"; and obligations which Columbia would undertake with respect to the filter.

Prior to the May 4, 1967, meeting, Columbia had independent tests performed by Fitelson Laboratories and these tests tended to support Strickman's claims concerning the effectiveness of the filters in reducing tars and nicotine gas. Taste tests were to be conducted in order to verify the effect of the filter on the natural flavor of the cigarette smoke.

Subsequent to these meetings, it was decided that the approximately 20 members of the Strickman group would need to act in concert at the time of the transfer, and thereafter, in dealing with Columbia. A power of attorney as a means of effecting the transfer was rejected because a pure agency relationship would be revoked by the death of any member of the group. In a letter dated June 6, 1967, to John Wheeler, an attorney for Columbia, Katz described the need for a vehicle for the transfer and stated that a trust would probably be utilized. The letter states:

> The Declaration of Trust will give to the Trustees legal title with all of the powers requisite to whatever action may be required in the future as well as the power to sell the patent to Columbia * * *.

Accordingly, on June 9, 1967, a trust agreement was executed between the Strickman group as grantors, and Strickman and Raum, as trustees, in which the grantors transferred all their rights in the filter to the trust. The trustees were to "collect the net income or proceeds of sale" and make distributions thereof to the grantors in accordance with specified percentages. The powers of the trustees were provided as follows:

TRUSTEES' POWERS

1. To sell to COLUMBIA UNIVERSITY or to any of its designees the entire right, title and interest in and to the INVENTION upon such terms as in their sole discretion and judgment may be deemed for the best interest of the beneficiaries hereunder.

2. To compromise, settle, arbitrate or defend any claim or demand in favor of or against the trust and to enter upon such contracts and agreements and to make such compromises or settlements of debts, claims or controversies as they may in their sole discretion deem necessary or advisable.

3. To incur and pay the ordinary and necessary expenses of administration, including (but not by way of limitation) reasonable attorneys' fees, accountants' fees, and the like.

4. To act hereunder through an agent or attorney-in-fact, by and under power of attorney duly executed by the Trustees, in carrying out any of the powers and duties herein authorized.

On June 9, 1967, the trust agreement was amended to provide that no beneficiary could assign his interest without the consent of the co-trustees, and that the co-trustees would not enter into any transaction affecting "the bulk of the property rights owned by the Trust" without the approval of at least 80 percent of the holders of beneficial interests in the trust property.

During June 1967, an assignment agreement between Columbia and the Strickman group was being drafted with Katz and Raum participating extensively in the drafting process. During this period, Columbia was considering whether it should enter the transaction. An ad hoc committee of trustees of the university and the investments subcommittee of the university's finance committee evaluated the prospects and advisability of consummating the transfer. Dr. Grayson Kirk, president of Columbia, forwarded to the trustees, for their consideration, a report of the finance committee favoring the proposal. The trustees were advised that:

> The holders of the invention would assign all of their right, title and interest in the patent application to the University * * * in exchange for a purchase price * * * to be paid periodically over a period approximating the life of the patent, which payments would be contingent on the amount of royalties received from the University's licenses * * *.

During this period the Strickman group was pressing Columbia for a decision. A decision in favor of accepting the transfer was reached, and negotiations between the university and the Strickman group, involving substantial bargaining, were finalized.

On July 7, 1967, an assignment by the trust of all its interest in the filter to Columbia and an assignment agreement between the trustees and Columbia were executed. The lengthy assignment agreement (hereinafter sometimes referred to as the "agreement") contained provisions dealing with the nature of the transfer, domestic and foreign patent applications for the invention and improvements thereon, limitations on disclosures of confidential information, payments to the trust, licensing of the patent to cigarette manufacturers, royalties, Columbia's obligations with respect to future litigation, and termination of the agreement.

The agreement stated:

> Assignors [the trustees] by these presents do hereby sell, assign and transfer unto Assignee [Columbia] the full and exclusive right * * * in * * * the Invention * * *.

Columbia agreed to negotiate nonexclusive licenses for the invention with cigarette manufacturers. The

agreement sets forth a schedule of fees to be charged the licensees, as well as royalty rates, minimum annual royalties, and an outline of the licensing agreement to be used by Columbia. From the gross receipts received by reason of Columbia's licensing of the invention, Columbia may deduct reasonable expenses for such purposes as research, litigation, maintenance of patents, and any other purpose necessary for developing the invention and maximizing its economic return. "Net royalties" was defined as the difference between gross receipts and expenses.

Columbia was required to keep full and accurate records with respect to all receipts and expenses employed to compute the "net royalties" and the trust retained the right to inspect such books and records.

The agreement further states:

> Assignee shall pay to the Assignors as compensation for the assignment of the Invention and other considerations expressed herein, the following percentage of net royalties received by it from the licensing of the patent and trademark rights:
>
> | | |
> |---|---|
> | Out of the first $5,000,000 | 90% |
> | Out of the second $5,000,000 | 80% |
> | Out of the third $5,000,000 | 70% |
> | Out of the fourth $5,000,000 | 60% |

Out of the fifth $5,000,000	50%
Out of all above $25,000,000	49%

[Emphasis added.]

Other obligations assumed by Columbia include the requirement that it defend the patent through defensive and offensive litigation, if necessary, and secure and maintain any desirable foreign patents. The agreement was to expire at the close of the calendar quarter in which the last of all the relevant patents expired, unless terminated earlier. The agreement described circumstances in which either party might choose to terminate the agreement: (1) In the event Columbia failed to comply with any provision of the agreement and such failure or breach continued uncured for a period of 60 days after written notice of the breach is received from the trust; and (2) in the event annual net royalties did not average at least $100,000 per year for any 3 consecutive calendar years beginning with 1971. If termination occurred, Columbia would reassign all rights in the invention to the trust.

The agreement was signed by representatives of Columbia and by the co-trustees, Raum and Strickman. The language of "sale" contained in the agreement was

inserted to substantiate the Strickman group's claim for "sale or exchange" treatment under section 1235 of their gain on the disposition of the patent. The tax treatment of the net royalty payment to the trust had been the subject of discussion at negotiations between Columbia and the Strickman group. In view of the concern that the payments be taxed at capital gains rates, no charitable deduction was anticipated at this time. The availability of a charitable deduction was not one of the reasons for approaching Columbia.

On July 13, 1967, Columbia issued several press releases describing the transaction, the invention, and the inventor. In addition, Dr. Grayson Kirk held a press conference in order to publicize the transfer. Columbia was very anxious about adverse publicity resulting from its association with an invention which might encourage cigarette smoking. The transfer was characterized in the press release as one designed primarily to aid cancer research as well as the university.

Columbia began to perform its obligations under the agreement and hired a manager to work exclusively on the filter. By early August 1967, sufficient doubts arose about the effectiveness of the filter to cause Columbia

to suspend all licensing activities until further tests were conducted. At that time, Dr. Kirk was called to testify before a United States Senate subcommittee with respect to the filter and Columbia's role in promoting it.

Columbia engaged the services of one of its most eminent chemists, Dr. Ralph Halford, to test the filter. Tests were conducted with the cooperation of the Strickman group. The Strickman group was not satisfied with the progress of the work and in mid-September gave notice of their intention to terminate the agreement. Formal notice of termination was served in January 1968, and by February 1968 Columbia ceased to have an interest in the filter.

On their 1967 income tax returns all the petitioners claimed charitable contribution deductions as a result of the transaction with Columbia. The amounts of the deductions were computed generally by multiplying one-half of a figure utilized as the value of the invention [4/] by the percentage interest allegedly owned by each petitioner. The value was based upon the price at which

---

4/ The use of one-half the value is founded on the allegation by petitioners that they gave one-half of their interest in the filter to Columbia.

certain interests in the invention allegedly had been sold. Petitioners claimed contributions in 1967 in the following amounts:

Petitioner	Amount
Robert S. Raum, et ux.	$ 450,000
Irving I. Rusoff, et ux.	56,500
William W. Suitt, et ux.	978,750
Robert Strickman, et ux.	1,734,300

Because of the percentage limitations in section 170, petitioners could deduct only part of the contributions. The remainder was utilized as a carry-forward of charitable contributions and was deducted by petitioners to the extent allowable in subsequent years.

OPINION

1. Ownership Issue

Respondent seeks to deny the claimed charitable contributions on the ground that, as a result of the June 9, 1967, transaction, the trust became the owner of the filter, and the trust rather than petitioners made the July 7, 1967, transfer to Columbia. He contends that, since petitioners had already transferred all their interest in the filter to the trust, they could not have made a charitable contribution to Columbia.

Respondent's argument is without merit. Under the terms of the trust created by petitioners on June 9, 1967, the trustees are directed to "collect the net income or proceeds of sale" and to "make distribution thereof upon receipt to the Grantors in accordance with the percentages appearing alongside their signatures or in accordance with any writing dated subsequent hereto." Under section 677(a)(1), 5/ the grantor of a trust is treated as the owner of any portion of a trust whose income may be "distributed to the grantor." Since the grantors of the June 9, 1967, trust were entitled to both the trust's income and the proceeds of the sale of the corpus, they are treated as the owners of the entire trust.

5/ SEC. 677. INCOME FOR BENEFIT OF GRANTOR.

(a) General Rule.--The grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under section 674, whose income without the approval or consent of any adverse party is, or, in the discretion of the grantor or a non-adverse party, or both, may be--

(1) distributed to the grantor or the grantor's spouse;

Section 671 provides that where the grantor shall be treated as the owner of any portion of a trust, "there shall be included in computing the taxable income * * * of the grantor * * * items of income, deductions, and credits against tax of the trust * * *." Accordingly, the grantors of the June 9, 1967, trust are entitled to take their respective proportionate shares of the trust's deductions in computing their taxable income. See William Scheft, 59 T.C. 428, 431-432 (1972); Archbishop Samuel Trust, 36 T.C. 641, 651 (1961), affd. 306 F.2d 682 (1st Cir. 1962).

That the grantors' deductions derived from the trust include the trust's charitable contributions is made doubly clear by the regulations. Sec. 1.671-3(a)(1), Income Tax Regs., provides that if a grantor is treated as the owner of an entire trust (corpus as well as ordinary income), he takes into account all items of income, deductions, and credit "to which he would have been entitled had the trust not been in existence during the period he is treated as owner." Sec. 1.671-2(c), Income Tax Regs., states:

> * * * a charitable contribution made by a trust which is attributed to the grantor (an individual) under sections 671 through

677 will be aggregated with his other charitable contributions to determine their deductibility under the limitations of section 170(b)(1).

Accordingly, any charitable contributions made by the June 9, 1967, trust would be deductible by petitioners. The issue remains, however, as to whether the trust made a "charitable contribution" of the filter to Columbia.

2. The Charitable Contribution Issue

Section 170 6/ allows as a deduction any "charitable contribution," payment of which is made during the taxable year. When the transfer at issue was made, a deduction was allowable under section 170 for a contribution of property, other than money, in an amount

---

6/ SEC. 170. CHARITABLE, ETC., CONTRIBUTIONS AND GIFTS.

(a) Allowance of Deduction.--

(1) General rule.--There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year. A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary or his delegate.

equal to its fair market value at the time of the contribution, sec. 1.170-1(c)(1), Income Tax Regs., and a gift of a patent could qualify as a charitable contribution. Rev. Rul. 58-260, 1958-1 C.B. 126. If the fair market value of the contributed property exceeded the allowable percentage of the taxpayer's adjusted gross income as computed for this purpose for the taxable year, such excess could be carried forward to the later years.

Petitioners contend that the trust's transaction with Columbia was a charitable contribution of one-half of the trust's interest in the filter and that, as settlors of a "grantor trust," 7/ they are entitled to the maximum percentage allowable charitable contribution deductions in 1967 and to the carryovers of the unused balance to later years. 8/ Respondent maintains, and we

---

7/ See secs. 671, 677; secs. 1.671-1, 1.671-3, Income Tax Regs.; William Scheft, 59 T.C. 428, 431-432 (1972); Archbishop Samuel Trust, 36 T.C. 641, 651 (1961), affd. 306 F.2d 682 (1st Cir. 1962).

8/ Petitioners compute their charitable contribution deductions by assigning a fair market value of approximately $20,000,000 to the interest in the filter transferred to Columbia. The issue as to the filter's value has been severed for separate trial.

agree, that the trust's transaction with Columbia was not a "charitable contribution" within the meaning of section 170(a) and, consequently, the claimed deductions are not allowable.

The term "charitable contribution" has been generally held synonymous with the term "gift." DeJong v. Commissioner, 309 F.2d 373 (9th Cir. 1962), affg. 36 T.C. 896 (1961); James A. McLaughlin, 51 T.C. 233, 234 (1968), affd. per order (1st Cir. May 28, 1969); Larry G. Sutton, 57 T.C. 239, 242 (1971). "A gift is generally defined as a voluntary transfer of property by the owner * * * without consideration therefor." Harold DeJong, 36 T.C. at 899; Larry G. Sutton, supra at 242. If the transfer is impelled primarily by the anticipation of some economic benefit or is in fact an exchange in the form of a substantial quid pro quo, it is not a contribution. Singer Co. v. United States, 196 Ct. Cl. 90, 105-106, 449 F.2d 413, 422 (1971); Stubbs v. United States, 428 F.2d 885, 887 (9th Cir. 1970), cert. denied 400 U.S. 1009 (1971); Rainier Companies, Inc., 61 T.C. 68, 77 (1973); Charles O. Grinslade, 59 T.C. 566, 577 (1973).

We must therefore inquire into what actuated petitioners in making the transfer to Columbia. The task is

not to measure the extent to which pristine charitable benevolence prompted the transfer. Cf. Commissioner v. Duberstein, 363 U.S. 278, 285 (1960). Rather, our inquiry seeks to expose the true nature of the transaction: Whether the gift was made "in expectation of the receipt of certain specific direct economic benefits within the power of the recipient to bestow directly or indirectly, which otherwise might not be forthcoming." Stubbs v. United States, supra at 887; Larry G. Sutton, supra at 243. The issue is factual.

As we view the evidence in its entirety, it clearly shows that the transfer to Columbia was a business transaction, not a charitable contribution. In essence, the Strickman group, acting through the trust, created a joint venture with Columbia for the profitable, commercial exploitation of the filter. The trust and Columbia negotiated an agreement which both of them hoped and expected to be mutually advantageous. From this transaction, we infer that petitioners expected to receive, directly and indirectly, financial benefits fully commensurate with the value of the property transferred. See Charles O. Grinslade, supra at 577. In no sense of the term as it is used in section 170(a) was the transaction a

"charitable contribution." Analysis of events surrounding the transfer and the legal documents executed by the parties confirm this conclusion.

At the time the assignment agreement with Columbia was negotiated, the filter had been invented but needed testing and refining. Exploitation of the invention was expected to be an expensive and highly speculative venture. The Strickman group was aware of its own lack of credibility, its weakness vis-a-vis the powerful cigarette manufacturers, and the need for further development of the patent. Association with Columbia, a prestigious educational institution with a superior, widely-known medical school, gave the filter valuable favorable publicity as well as credibility as a cancer deterrent. It also provided the leverage needed for dealing with the tobacco industry in developing a market for the filter. It was with these needs and potential benefits in mind that the Strickman group negotiated the transfer to Columbia.

The July 7, 1967, assignment agreement itself reflects an arrangement for the mutual advantage of the parties, a quid pro quo, not a charitable contribution. The agreement provides that the trustees "hereby sell, assign and transfer" (emphasis added) the invention to

Columbia. At its own expense, Columbia agreed to prosecute the patent applications to issuance or rejection and to file and prosecute corresponding foreign patent applications in "such countries as it reasonably deems necessary in order to obtain the greatest revenue from its ownership of the Invention." Columbia undertook to "attempt to negotiate nonexclusive licenses, to manufacture, use or sell the Invention, with manufacturers of cigarettes, manufacturers of cigarette filters," and others throughout the tobacco industry. The agreement specified the minimum license and other fees to be charged. In addition, Columbia undertook at its own expense to protect the patent from infringement.

As "compensation for the assignment of the Invention and other considerations expressed" the Strickman group was to receive substantial and direct pecuniary benefits. Moreover, the Strickman group was to be relieved of negotiating and policing all licensing agreements as well as perfecting and protecting all patents, domestic and foreign. The trustees were to receive the percentages of the net royalties (ranging from 90 percent of the first $5,000,000 to 49 percent of all amounts above $25,000,000) set forth in our Findings--income earned, in large part,

by Columbia's reputation and efforts. In the event the net royalties should not average at least $100,000 per year for any 3 consecutive calendar years beginning with 1971, and in other specified circumstances, the trust could give notice of termination of the agreement, and Columbia would be obligated to reconvey the filter to the trust. Indeed, because the trustees were dissatisfied with Columbia's initial steps in carrying out the agreement, the trustees gave notice of termination in mid-September 1967, less than 3 months after the agreement was signed--an action hardly consistent with a genuine donative intent.

The June 9, 1967, trust agreement executed less than a month before the agreement with Columbia does not even purport to authorize the trustees to make a gift of the trust property but, instead, empowers them to "sell" the invention to Columbia or any of its designees. The treasurer of Columbia testified that he "wanted the transfer to go through" because he "looked on it as a favorable business transaction for the university." As pointed out in our Findings, the language of the trust agreement with Columbia was carefully chosen with a view to obtaining the favorable "sale or exchange" treatment

of patent income under section 1235. Every legal document executed in this whole transaction is phrased in the terms of a sale.

In sum, the tenor and content of the negotiations, the language of the documents of transfer, and all the surrounding facts are inconsistent with a genuine donative intent and are consistent with only one conclusion--this was a purely business transaction with no charitable element. See Charles O. Grinslade, supra at 577; Rainier Companies, Inc., supra at 77.

Petitioners dispute this conclusion, citing testimony that the parties intended in some way to give approximately half their interest to Columbia or that, if there was a sale, it was a bargain sale of the invention to Columbia with a contribution equal to the bargain element. In the face of cogent documentary evidence, petitioners now repudiate the work of their lawyers as inconsistent with their intentions and the substance of the transaction. We find no merit in these arguments.

All the petitioners, excluding Rusoff, were present at the meetings with Columbia where the format of the transaction and section 1235 capital gains treatment were discussed. Katz, who was the moving force behind

the transfer, and Raum, an attorney and leading member of the Strickman group, both participated in the drafting of the documents. Both were undoubtedly aware of the group's intention and what the group wanted accomplished. All the petitioners signed the trust agreement. Petitioners cannot be heard to disavow the efforts of their attorneys and other representatives acting on their behalf and dismiss these "formalities" as mere "lawyers' doings."

As far as we can tell from the evidence, the theory of a charitable contribution was an afterthought which was not conceived until after the mid-September notice of termination had been sent to Columbia, the spectre of the venture's failure was apparent, and, possibly, not until petitioners' 1967 returns were being prepared. This was too late. The history of a business transaction entered into with the hope and expectation of what one witness described as "astronomical" profits flowing to the trust cannot be rewritten to reflect a benevolent, charitable plan which unexpectedly failed.

Petitioners have simply failed to convince us that this transaction had any element of charity. True, both of Strickman's parents died of cancer, and he professed

an interest in Columbia's cancer research. Raum testified he was willing to give to Columbia what he anticipated would be millions of dollars because his wife attended some graduate courses there. Suitt's daughter attended Columbia's school of general studies for a limited period of time. Rusoff was aware of Columbia's good work. These motivations are not commensurate with the generosity petitioners claim, especially when it is remembered that a notice of termination was sent to Columbia during the period the filter was being tested and within less than 3 months after the agreement was signed.

We do not doubt that petitioners intended to confer an economic benefit upon Columbia, nor that at least some of the petitioners hoped that Columbia would use the funds to further cancer research. However, the expected economic benefit to Columbia is identical to that conferred upon any person chosen to render services in return for compensation. That intention is insufficient to characterize the transfer as a charitable contribution within the meaning of section 170(a).

The issues decided above were severed for a separate trial by order dated March 13, 1974. Our conclusions

herein obviate the necessity for a trial of the issue as to the valuation of the filter at the time it was transferred to Columbia. The Court has not been advised, however, as to the disposition of other pleaded issues. The parties will be expected to file appropriate motions for the further handling of these cases.

Appropriate orders will be issued.

UNITED STATES TAX COURT

IRVING I. RUSOFF and PERLE P. RUSOFF, Petitioners,	)	
v.	)	Docket No. 682-72
COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed December 2, 1975, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in income tax due from the petitioners for the taxable year 1967 in the amount of $1,184.97.

(Signed) C. Moxley Featherston

Judge.

Entered: JUN 30 1976

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

ROBERT S. RAUM
Counsel for Petitioners
210 East 52nd Street
New York, New York 10016

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

(Sgd) EDWARD H. HANCE-J S H

By: _____
EDWARD H. HANCE,
Act'g. Asst. Regional Counsel
26 Federal Plaza (12th Floor)
New York, New York 10007,
Tel. No. 212-264-0273.

JUN 8 1976

UNITED STATES TAX COURT

ROBERT STRICKMAN AND ROSE STRICKMAN,	)	
Petitioners,	)	
v.	)	Docket No. 1358-72
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed December 2, 1975, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there are deficiencies in income taxes due from the petitioners for the taxable years 1967 and 1968 in the amounts of $3,416.92 and $6,148.90, respectively.

Judge.

Entered: JUN 30 1976

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

/s/ Robert S. Hatch
ROBERT S. HATCH
Counsel for Petitioners
210 East 52nd Street
New York, New York 10016

By: (Sgd) EDWARD H. HARCH
EDWARD H. HARCH,
Act'g. Asst. Regional Counsel
26 Federal Plaza (12th Floor)
New York, New York 10007,
Tel. No. 212-264-0273.

JUN 4 1973

[-2-]

BEST COPY AVAILABLE

UNITED STATES TAX COURT

WILLIAM W. SUITT and KATHRYN S. SUITT,	)	
Petitioners,	)	
v.	)	Docket No. 1724-72
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed December 2, 1975, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there are deficiencies in income taxes due from the petitioners for the taxable years 1967, 1968 and 1969 in the amounts of $1,026.39, $5,592.23 and $815.00, respectively.

C. Clarkey Fos

Judge.

Entered:

JUN 30 1976

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

/s/ Robert S. Raum
ROBERT S. RAUM
Counsel for Petitioners
210 East 52nd Street
New York, New York 10016

By: (Sgd) EDWARD H. HANCE-J S H
EDWARD H. HANCE,
Act'g. Asst. Regional Counsel
26 Federal Plaza (12th Floor)
New York, New York 10007,
Tel. No. 212-264-0273.

JUN 6 1975

UNITED STATES TAX COURT

ROBERT S. RAUM and RUTH RAUM,	)	
Petitioners,	)	
v.	)	Docket No. 2212-72
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed December 2, 1975, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there are deficiencies in income taxes due from the petitioners for the taxable years 1967, 1968 and 1969 in the amounts of $3,887.00, $6,059.00 and $7,129.00, respectively.

(Signed) C. Moxley For
Judge.

Entered: JUN 30 1976

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

/s/Robert S. Raum
ROBERT S. RAUM
Counsel for Petitioners
210 East 52nd Street
New York, New York 10016

MEADE WHITTAKER,
Chief Counsel,
Internal Revenue Service.

(Sgd) EDWARD H. HANCE-J S H

By: _____
EDWARD H. HANCE,
Act'g. Asst. Regional Counsel
26 Federal Plaza (12th Floor)
New York, New York 10007,
Tel. No. 212-264-0273.

JUN 8 1976

UNITED STATES TAX COURT

IRVING I. RUSOFF and PERLE P. RUSOFF, Petitioners,	)	
v.	)	Docket No. 3740-72
COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed December 2, 1975, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in income tax due from the petitioners for the taxable year 1968 in the amount of $1,999.60.

Judge.

Entered: JUN 30 1976

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

/s/Robert S. Raby
ROBERT S. RABY
Counsel for Petitioners
210 East 52nd Street
New York, New York 10016

By: (Sgd) EDWARD H. HANCE-J S H
EDWARD H. HANCE,
Act'g. Asst. Regional Counsel
26 Federal Plaza (12th Floor)
New York, New York 10007,
Tel. No. 212-264-0273.

JUN 8 1976